HARVARD ManageMentor

Performance Measurement

About this Topic: Performance Measurement

Topic Mentor

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His fourth book co-authored with David Norton, *Alignment*, will be published in February 2006. His previous books with Norton include *Strategy Maps: Converting Intangible Assets into Tangible Outcomes*, named as one of the top ten business books of 2004 by *Strategy & Business* and amazon.com; *The Strategy-Focused Organization: How Balanced Scorecard Companies Thrive in the New Business Environment*, named by Cap Gemini Ernst & Young as the best international business book for year 2000; and *The Balanced Scorecard: Translating Strategy into Action*, which has been translated into 22 languages and won the 2001 Wildman Medal from the American Accounting Association for its impact on the practice of accounting.

Topic Source Notes

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What Would You Do?

What would you do?

Maura's thrilled about her recent promotion to manager of a product group at TopCo's London division. But a week into the new job, her boss, Tina, calls a meeting with all the group leaders from the division. At the meeting, she explains that she wants to make some changes in how the division is assessing its business performance. "We've been focusing too much on the numbers," she says. "I need a more comprehensive picture of the value our division is generating."

Tina challenges the group leaders to reexamine how they're currently assessing their groups' performance, and to propose ideas for change. Maura leaves the meeting unsure of where to begin.

What would you do?

Maura should first ask Tina to clarify TopCo's and the division's strategies. Maura realizes that the different ways they gauge success at TopCo work together like a dashboard, showing the state of the company. Based on her understanding of her division's strategy, she and her group will then identify appropriate objectives (or goals) for the group. Next, they'll work together to identify the two or three critical activities they must carry out to achieve those objectives. And they'll translate those actions into a set of performance metrics that express how they'll measure progress on the critical activities. Their metrics will need to reflect a mix of business results—such as sales, customer satisfaction, product innovation, best-practice sharing, staff morale, and operational efficiency. Once Maura's group has created metrics, they will set targets representing the division's desired performance on each metric—and begin gathering data to see how their actual performance compares with the targets they've set. They'll then analyze any gaps between actual and target performance—and decide how to respond.

In this topic, you'll learn how to apply this same process to measure your own group's performance.

Often managers need to assess both financial *and* non-financial performance. What process would you use to measure things that are not easily quantifiable?

Topic Objectives

This topic helps you:

- Understand the importance of regularly measuring your group's performance
- Gain familiarity with formal performance measurement systems
- Apply a disciplined process to performance measurement
- Avoid common performance measurement pitfalls
- See how measuring your group's performance can help you better manage that performance

Keeping score

Do you jog, play basketball, ride a bike, or participate in some other team or individual sport? If so, you likely keep track of your performance—even if it's as simple as "I ran that eight-mile loop faster than ever!" or "I scored four more points during this game than I did in the last one."

Why do you keep score in these ways? Like many people, you're probably performance-driven or achievement-oriented—or maybe just naturally competitive. You want to know whether your performance is improving or declining and how your latest achievement compares with your personal best. You crave feedback on how you're doing.

In much the same way, organizations want—and need—to track the changes in their overall performance. And the divisions, units, teams, and individuals within them engage in similar scorekeeping.

Why measure business performance?

> “ You can't manage what you can't measure. ”
> –Peter Drucker

Organizations measure their performance for numerous reasons. Here are just a few:

- **Improvement:** By tracking performance, companies can spot—and promptly address—problems such as declining customer loyalty, flattening profits, or defections of talented employees.
- **Planning and forecasting:** Performance measurement serves as a progress check—enabling organizations to determine whether they're meeting their goals and whether they need to revise their budgets and forecasts.
- **Competition:** When companies compare their performance against their rivals' and against industry benchmarks, they can identify weak areas and address them to sharpen their competitive edge.
- **Reward:** By knowing how much employees have excelled in achieving goals, managers can distribute performance-based incentives and rewards fairly to their direct reports.
- **Regulatory and standards compliance:** Many companies measure performance in order to comply with government regulations (such as antipollution laws) or international standards (for instance, ISO 9000).

What is performance measurement?

In its simplest terms, measuring performance means assessing business results to: (1) determine how effective a company's strategies and operations are and (2) make changes to address shortfalls and other problems.

Companies measure their performance using different methods and criteria. However, in many organizations, performance management entails examining the results generated by key business activities, using specific **performance metrics** (also known as measures). For each business activity, there are numerous possible metrics. The table below shows just a few examples.

Specific Performance Metrics

Business Activity	Possible Performance Metrics
Finance	• Profit margin (percentage of every dollar of sales that contributes to the company's bottom line) • Revenues
Marketing	• Market share • Customer profitability
Production	• Number of units manufactured within a specific time period • Number of items shipped on time • Machine changeover time
Sales	• Percentage of customer visits or phone calls that generate sales • Percentage increase in sales over previous quarter or year • Percentage of customers retained this period
Customer Service	• Number of customer complaints • Service-call response time

Purchasing	• Vendors' ability to provide services or materials on time • Defect rate of vendors' products
Quality	• Product yield: ratio of good products produced to total products started into production • Defect rates of a key process
Human Resources	• Workforce turnover • Absenteeism rates

Key Idea: The importance of balance

Key Idea

Many organizations use a coordinated system, or framework, to measure business performance across their functions. The best performance measurement systems demonstrate balance.

- They assess a company's financial performance (such as revenues, expenses, and profits) and nonfinancial performance (for example, employee knowledge, information system availability, and quality of customer relationships).
- They draw on internal data (such as process quality) and external data (for example, third-party rankings of companies' product performance against competitors').
- They examine lagging (backward-looking) indicators and leading (forward-looking) indicators. For instance, sales figures show you what your company has achieved in the past, and thus are a lagging indicator. By contrast, customer-satisfaction ratings suggest how your customers may behave in the future; thus they constitute a leading indicator.
- They weigh both subjective (difficult to quantify) aspects of performance (such as customer satisfaction and employee capabilities) and objective (easy to quantify) aspects (for example, revenues and return on invested capital).

Balance is key to a strong performance measurement system.

A comprehensive picture

By striking a balance in its performance measurement system, a company compiles a more complete picture of how it's doing. This comprehensive picture enables executives and managers to learn from mistakes, constantly improve, and make the smartest possible decisions.

Indeed, some managers draw an analogy between effective performance measurement and the operation of an airplane: To fly a plane, a pilot must look at many instruments—airspeed indicator, fuel gauge, altitude indicator, GPS map, and so forth—rather than rely on a single instrument that provides

just one piece of information. Similarly, organizations seeking to navigate through a complex environment need a range of "instruments" to evaluate how they're doing. Effective performance measurement provides that comprehensive range of information with which a company can gauge its performance.

Who uses the data?

Many people inside and outside a company use performance measurement data.

- **Executives** use the data to review how well corporate strategy is being implemented and whether major corrective actions need to be taken.
- **Unit managers and group leaders** use performance data to motivate and evaluate employee performance and productivity.
- **Shareholders, industry analysts, customers, media, and government regulators** use data to make choices such as whether to invest in or buy from a company, or to determine whether an organization is operating with efficiency and integrity.
- **Employees** learn whether they and their teams are contributing to company goals.

Where do you fit in?

Does your boss require you to track specific aspects of your group's performance? If not, should you still take time to learn about performance management and measure your group's business results? The answer is "Yes!" Why? Assessing your group's results—and understanding the value of performance measurement in general—enables you to:

- Determine whether you and your direct reports are helping your company to achieve its goals
- Correct any missteps or flaws in order to improve your group's performance
- Understand how your behavior and choices affect your employees' performance
- Identify new opportunities for your unit or group to improve its effectiveness or even extend its contribution to the company's success
- Build your business knowledge and professional credibility—and thereby further your career

A tool to assess performance

Some companies have formal, enterprise-wide performance measurement systems in place (such as Six Sigma, the Plan-Do-Check-Act methodology, or the Balanced Scorecard). Such systems enable executives to look across the organization's business activities to gain a holistic view of the company's performance. Other companies use a simpler approach, measuring the performance of one or more discrete aspects of the business.

Regardless of the system a company uses, all organizations use key performance indicators (KPIs) to assess their performance.

Key Idea: What is a KPI?

Key Idea

A **key performance indicator** (**KPI**) is a measure reflecting how an organization is doing in a specific aspect of its performance. A KPI is one representation of a **critical success factor** (**CSF**)—a key activity needed to achieve a given strategic objective. Organizations that measure performance identify the handful of critical success factors that comprise every strategic objective.

> For example, depending on a company's strategy, the organization might have a KPI for the percentage of income the organization derives from international markets. Another KPI might be the number of customer complaints about orders filled incorrectly. Some organizations use many KPIs, for all their different areas of operation. Other enterprises' KPIs may focus on a specific area. For instance, a social service nonprofit may focus all its KPIs on the amount of aid that is granted to different entities.

Typically, each unit within a company also has a set of KPIs that support the company's goals. Performance data for a unit's KPIs can be rolled up into the company's KPIs to reflect total organizational performance in any given area being measured.

You probably won't participate in developing KPIs at the corporate level. However, you may be involved in creating KPIs at your unit's level—especially if your unit was recently acquired or has been associated with a new product, process, department, or line of reporting. Regardless of your situation, you should be aware of the KPIs that are in place in your organization. With this awareness, you can measure your and your group's progress towards corporate and unit goals.

Understanding KPIs can help you measure your and your group's progress toward corporate and unit goals.

Three types of KPIs

Key performance indicators come in three types:

- **Process KPIs** measure the efficiency or productivity of a business process. Examples include "Product-repair cycle time," "Days to deliver an order," "Number of rings before a customer phone call is answered," "Number of employees graduating from training programs," and "Weeks required to fill vacant positions."
- **Input KPIs** measure assets and resources invested in or used to generate business results. Examples include "Dollars spent on research and development," "Funding for employee training," "New hires' knowledge and skills," and "Quality of raw materials."
- **Output KPIs** measure the financial and nonfinancial results of business activities. Examples include "Revenues," "Number of new customers acquired," and "Percentage increase in full-time employees." Three particularly common output KPIs that are used by managers include:

- **Return on investment (ROI):** Return on investment represents the benefits generated from the use of assets in a company, unit, or group—or on a project. ROI is helpful to top executives, finance managers, board members, and shareholders. A possible way to express return on investment is to divide net income (revenues less expenses less any liabilities, such as taxes) by total assets. ROI measures how effectively managers have used resources, and can be figured as follows:

ROI = Net Income/Total Assets

- **Economic value added (EVA)™:** EVA, popularized in the 1990s by U.S. management consultancy Stern Stewart & Co., is defined as the value of a business activity that is left over after you subtract from it the cost of executing that activity and the cost of the physical and financial capital deployed to generate the profits. In the field of corporate finance, EVA is a way to determine the value created, above the required return, for a company's shareholders. It's therefore useful to senior management, boards, and shareholders and other investors. EVA is calculated as follows:

  EVA = Net operating profit after taxes minus (net operating assets multiplied by the weighted average cost of capital)

  Shareholders of a company receive a positive EVA when the return from the equity employed in the business's operations is greater than the (risk-adjusted) cost of that capital.

- **Market share:** The percentage of sales in a given industry segment or sub-segment captured by your company.

All three types of KPIs—process, input, and output—generate valuable performance information. A mix of the three types ensures a comprehensive picture of your unit's or organization's performance.

Activity: Pick the right KPI

Different aspects of business performance call for different KPIs. Choose the right KPI for the particular aspects of performance you want to measure.

You want to measure the efficiency of the various business processes used in your department. Which one of the following represents a KPI that would help you gauge a process's efficiency?

- ○ Percentage increase in revenues

  Not the best choice. This KPI would help you measure the financial results of your department's business activities (including selling and marketing efforts), not the efficiency of processes used in your department.

- ○ Funding approved for market research

  Not the best choice. This KPI would help you measure resources allocated to generating business results; in this case, funding dedicated to market research designed to produce knowledge of customer preferences.

- ○ Number of weeks to fill an open position in the department

  Correct choice. This KPI would help you measure the efficiency of your recruiting and hiring processes.

As the recently promoted head of your division, you'd like a clearer sense of how assets are being invested to generate important business outcomes. Which one of the following represents a KPI that would give you this kind of information?

- Number of customers who buy additional products after their first purchase

  Not the best choice. This KPI would help you measure the efficiency of a process (in this case, your customer loyalty efforts), not the assets used to generate business results.

- Employees' technological expertise

  Correct choice. Employees' technological expertise is an asset that, when used wisely, can help your division achieve valuable business results—such as development of innovative new products or services.

- Percentage of sales in your industry captured by your company

  Not the best choice. This KPI represents market share, which measures a nonfinancial result of business activities, not the assets used to generate business results.

Your boss has announced a new plan to improve understanding of the financial and nonfinancial results generated by the company's various business activities. Which one of the following would most likely generate the kind of information your boss wants?

- Budgetary resources devoted to community outreach by your department

  Not the best choice. This KPI would help you measure the assets and resources used to generate business results—in this case, dollars invested in outreach programs that enhance your company's reputation in the community. It would not help you quantify financial or nonfinancial results (change in public awareness and perception of your company) produced by these activities.

- Number of people a customer must speak with before having his or her problem or complaint solved

  Not the best choice. This KPI would help measure the efficiency of your customer service process. It would not enable you to quantify financial or nonfinancial results (customer satisfaction with the customer service process) generated by your department's activities.

- Percentage increase in the number of employees who stay longer than one year

  Correct choice. This KPI would help you measure the results (in this case, nonfinancial) of your employee loyalty activities.

KPIs and you

> "If you're not keeping score, you're only practicing, not playing."
> –Vince Lombardi

Even if your boss doesn't require you to track process, input, or output KPIs, it's vital that you familiarize yourself with these indicators—for several reasons:

- You may hear these terms used frequently in your organization.
- You want to understand how your organization defines the determinants of success—for example, where your organization's resource allocation emphasis is.
- In many industries, third-party researchers (such as J.D. Power & Associates) use KPIs to track how your company measures up against the competition. If you consult such research, you'll need to understand KPIs.
- These indicators can help you figure out your role in helping your organization achieve its goals.
- Plus, you'll enhance your credibility and value as a manager if you can demonstrate understanding of your company's and unit's KPIs.

KPIs in action

Who uses KPIs? Managers at all levels in an organization can track key performance indicators to assess how well their groups are meeting their business objectives, whether performance is improving or declining, and how their group's performance compares with that of other units or groups within the company and in rival organizations.

Consider these examples:

- A CEO examines return on investment (ROI) by division, or her company's cash flow, by month and quarter, and compares the results to those of competitors.
- A customer service manager tracks customer service quality using surveys. If the surveys suggest that service quality is dropping, he might need to add more account representatives to improve service levels.
- A benefits administrator monitors how many claims her group has processed during the current year, and compares it with the number processed in the previous year. An increase, for example, may suggest it's time to invest in new benefits software that can speed up claims processing.
- A product development manager assesses the ratio of sales from new products to total sales. He decides that his group needs to invest more in research and development to increase the ratio.
- A human resources staffer calculates the percentage of employees who actually attend voluntary training programs offered by the company, and compares the result against the targeted percentage. A drop may indicate the program is unsuccessful and can prompt an inquiry to find out why—possibly saving the company thousands of dollars in ineffective training programs.
- A communications expert reviews employee survey results to see whether workers understand the company's corporate strategy. Lack of understanding may suggest the need for clearer presentations on strategy by the company's CEO and other executives or the need to reach employees through different channels.

If you've recently started in your role as manager, you may not yet know which KPIs are used in your unit or group. How might you find out? Ask your boss what measures your group has been using to track performance. If your unit has a business analyst, see if he or she would be available to discuss your unit's KPIs and other performance metrics.

Key Idea: What is a performance measurement system?

Key Idea

Like many organizations, your company may be using a formal **performance measurement (PM) system**—a set of strategic objectives and performance metrics (including KPIs) applied throughout the entire enterprise. PM systems enable executives to see how business results generated in the company's many different units combine to influence the enterprise's overall results.

Thus, a PM system gives executives and managers a comprehensive, high-level view of their organization's performance—and an understanding of how the company's different parts work together to produce business results.

In many companies that use a PM system, senior executives advocate adoption of the system and manage its implementation. But once the system has been established, all managers and employees in the organization contribute to and use it. But how? They define individual goals that support unit- and company-level goals, and they generate performance data that their supervisors then input into the system.

How can you get a comprehensive view of how your organization is performing? Through a Performance Measurement system.

Benefits of a PM system

Performance measurement systems offer numerous benefits. Most important:

- **They enable managers to define (and track performance on) metrics for every strategic objective set by their unit and company.** By noting performance that falls short of targets (for example, "Our goal was to reduce order-processing errors 10%, but we only reduced them 5%"), managers can address the causes of the shortfall and work to continually improve performance.
- **They show how performance in different parts of the company affects performance in other parts.**

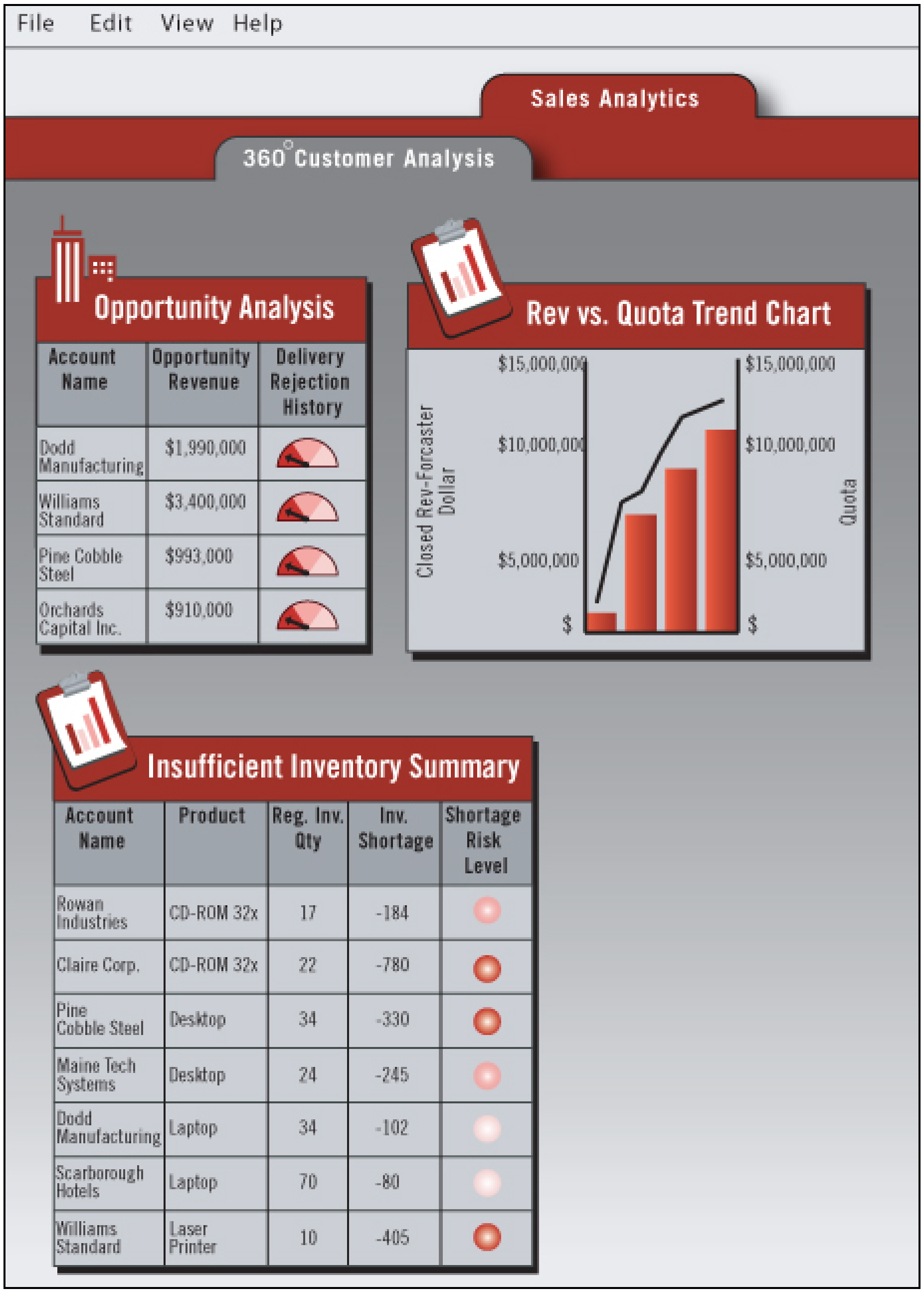
  For example, a company may discover that having the logistics staff achieve the objective "Accelerate order-delivery time by 10%," helps the customer service group meet its objective "Increase customer satisfaction by 15%."

By seeing these interrelationships, companies can make more informed decisions. For instance, they can increase a budget, add new hires, or introduce a more efficient process to improve performance—instead of guessing which factors need to be addressed.

Dashboards

Possibly the simplest type of PM system, a **dashboard** or **cockpit** combines the company's numerous metrics, targets, and performance data into one online or printed document (such as a spreadsheet) that's prepared monthly, quarterly, or on some other schedule.

Here is an example of a dashboard:



A dashboard enables executives and managers to easily digest the company's aggregated performance data. In addition, many dashboards use a "traffic light" coding system to evaluate performance on each metric, enabling leaders to spot and address problems promptly.

> For example, red indicates performance that's significantly below target; yellow, slightly below target; green, at or above target.

While dashboards have traditionally been used primarily by executives, many companies are now customizing their dashboards for managers at operational levels as well.

> For instance, at an airline, a manager in charge of stocking meals on board may see a different dashboard than the manager who oversees fuel purchasing. But each manager's customized dashboard also shows which planes are flying where.

Quality-improvement systems

Quality-improvement systems come in many different forms—including the following:

- **Plan-Do-Check-Act.** Popularized by total quality management (TQM) founder Dr. W. Edwards Deming, the Plan-Do-Check-Act framework helps managers establish a cycle of continuous improvement. The cycle comprises these steps: (1) *Plan:* Identify a performance problem and the processes affecting it. (2) *Do:* Explore potential solutions and implement one. (3) *Check:* Assess how well your solution worked. (4) *Act:* If your solution worked well, institutionalize it and look for another improvement opportunity. If it didn't, return to step 1.
- **Six Sigma.** With roots tracing back to the 1920s, Six Sigma is a data- and measurement-driven approach that helps managers continually improve business processes through reduction of errors. Many companies that use Six Sigma apply it to all their business processes—manufacturing, product development, order fulfillment, customer service, and so forth.
- **Baldrige National Quality Program.** Established in 1987 by a congressional act, the Baldrige National Quality Program was developed by the United States' National Institute of Standards and Technology. (The program is named after Malcolm Baldrige, who served as secretary of commerce from 1981 until 1987.) The Baldrige program defines criteria for high-quality business performance in numerous areas—such as leadership, strategic planning, customer focus, and knowledge management. The Baldrige framework has a European equivalent: The European Foundation for Quality Management. Every year, companies can apply for the Malcolm Baldrige Award, which recognizes organizations for achievement in specific categories: manufacturing, small business, education, and health care.

Balanced scorecard

Introduced in 1992 by Harvard Business School professor Robert Kaplan and Dr. David Norton, a management consulting firm head, the **Balanced Scorecard** (**BSC**) system recognizes that financial performance is just one part of the larger picture of organizational performance. The system seeks to balance a company's financial "perspective" with three nonfinancial "perspectives": customer, internal processes, and workforce learning and development. Companies that implement the BSC methodology develop and use two powerful tools:

- **Strategy map:** A one-page document, a strategy map graphically depicts executives' theory of the organization's strategy and the cause-and-effect relationships among the four scorecard perspectives. It shows the strategic objectives of each perspective and how they will affect performance on objectives in other perspectives. Many companies develop a corporate-level strategy map as well as strategy maps for each division, unit, and department. These lower-level maps contain objectives supporting the high-level map.

An example of a strategy map is as follows:

Image adapted from Robert S. Kaplan and David P. Norton, *Strategy Maps: Converting Intangible Assets into Tangible Outcomes.*

- **Scorecard:** The scorecard contains the metrics, targets, and actual performance data for each objective on the strategy map. Companies have a corporate-level scorecard that links down to lower-level business and support unit scorecards. Organizations often automate their scorecards with special software: When unit managers input data into their scorecards, the data are automatically aggregated into the high-level scorecard to show overall company performance. Software also allows managers to distribute and analyze reports easily.

Adopted by corporations, not-for-profit organizations, and public-sector entities (including government agencies, municipalities, and military forces), the BSC has become widely used for strategy execution.

Leadership Insight: Mission and objectives

We introduced the balanced scorecard in about 1990 - 1991 and within a few years several companies had gone forward and implemented the system with quite a bit of success. I went back to do some research on these early adopters and learned that the CEOs of two of these early adopters were former Marine officers.

Now, I used to be an engineer, and when I was an engineer if you got one unusual result you attributed it to experimental error but two was an example of a new theory. I thought, wow, this must be some interesting theory here, that's too much of a coincidence.

So I went back to both of those CEOs and told them about each other and asked them was there anything about their former life in the Marines that caused them to adopt the balanced scorecard—this performance measurement system—so effectively in their organizations?

Both of them gave me the same answer. They hadn't thought of it until I mentioned it, but they said the number-one responsibility for any Marine officer is communication. When they send the soldiers into battle, the general is not there with them. The soldiers are typically doing a very hazardous assignment and despite doing a ton of planning, whatever they plan doesn't happen. The lieutenant gets shot; the equipment is dropped off in the wrong spot; the enemy is in a different position and the troops can't call back and say, "Hey, boss, it ain't working — what should I do now?"

And they said, "Before we send any soldier into battle, we make sure every one of them knows the mission and the objectives. That's our number-one priority. And then in the heat of battle, they regroup and they do what's necessary to achieve the mission and the objectives." It's very interesting. When these former Marine officers became high-level executives, they were looking for a similar tool to get every employee in the organization aware of what the mission and the objectives are.

Because when a customer comes in for a transaction or when an employee is operating a very complex manufacturing process, the CEO is not there. He or she is dependent on that employee understanding not what they're supposed to do, but what they're there to accomplish, how they can contribute to the success of the organization.

And so these two CEOs found the balanced scorecard a very powerful and useful system to help them clearly communicate mission and objectives to every employee so that they all could understand it and they could all participate in helping the organization to accomplish its strategic objectives.

Effective performance measurement systems articulate strategic objectives, enabling leaders at all levels to make critical decisions.

Robert S. Kaplan
Professor, Harvard Business School

Robert S. Kaplan is Baker Foundation Professor at the Harvard Business School and Chairman, Professional Practice, at Palladium Group Inc. Before joining the HBS faculty in 1984, Robert was the Dean of the business school at Carnegie-Mellon University.

His research, executive education teaching, and consulting focus on linking cost and performance management systems to strategy implementation and operational excellence. Robert is a co-developer of both activity-based costing and the Balanced Scorecard.

He has authored or coauthored 14 books and approximately 150 papers, including 20 featured in Harvard Business Review. Recent books include "The Execution Premium: Linking Strategy to Operations for Competitive Advantage," the fifth Balanced Scorecard book coauthored with David Norton, and "Time-Driven Activity-Based Costing" with Steve Anderson.

In 2006, Robert was elected to the Accounting Hall of Fame. He received his Bachelor of Science and Master of Science in electrical engineering from MIT, and a doctorate in operations research from Cornell University.

Which PM system does your organization use?

If you don't know whether your organization has adopted a PM system or which system it uses, how do you find out? The quickest way is to ask your manager. In addition, many organizations publish articles about their PM system in company newsletters and refer to it in their annual reports and other publications. In some organizations, an internal performance measurement team provides training on the system to existing employees and new hires.

Look to all these sources for information if necessary. And listen for mention of a particular PM system while attending CEO speeches and all-staff meetings.

Key Idea: Make performance measurement part of your job

Key Idea

Whether or not your organization has adopted a company-wide performance measurement system, you can generate important benefits for your business by making performance measurement a regular part of your job. How? When you assess your group's results and uncover the causes behind troubling changes in your results, you can engineer the interventions needed for your group to improve its performance—and thus help the company generate better overall results.

How might you use measurement to better manage your group's performance? You first need to understand the performance measurement process. The performance measurement process unfolds over three phases. In phase one, you decide what you want to measure. In phase two, you gather performance data. And in phase three, you interpret the data you collected.

Assessing your group's results—and understanding the value of performance measurement in general—is part of every manager's job.

Phase 1: Decide what to measure

In this phase, you:

- **Define your objectives**

  For example, "Increase customer satisfaction," "Decrease on-the-job accidents," or "Cut expenses."

- **Define critical success factors (CSFs)**—the component parts of successfully achieved objectives; in other words, the actions that must be taken collectively to achieve a given objective

  For example, CSFs for the objective "Increase customer satisfaction" might include "Reduce sales staff turnover" and "Improve on-time delivery performance."

- **Define performance metrics**—the measures you'll use to assess whether you're accomplishing your CSFs

  For example, "Average length of salesperson tenure in department," "Number of sales staff departures per quarter," and "Percentage of orders delivered within +/- six hours of promised delivery time."

Phase 2: Gather performance data

During this phase, you:

- **Set targets for each metric**

  For instance, "An 8%-10% reduction in sales staff turnover during the second half of our fiscal year," and "98% of orders delivered on time."

- **Collect performance data**

  For example, count the number of sales staff who left the company during the final six months of the company's fiscal year, and record the delivery time of all orders during the past quarter.

Phase 3 interpret performance data

In this phase, you:

- **Analyze performance data**

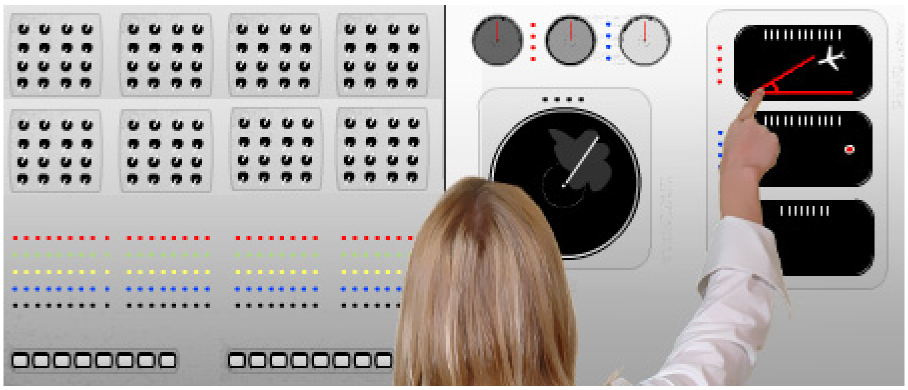
  For example, monitor the number of sales staff departures that occur each quarter, and determine whether you're on track to reduce turnover 8%–10% as planned. In analyzing the data, you'll want to examine the documented reasons for sales staff departures. For

example, dismissal, transfer to another department, acceptance of a similar position at a competitor, or retirement.

- **Test your measurement system**

  For instance, ask whether any metrics should be changed to more accurately represent the objective you're trying to achieve, or whether targets have been set at appropriate levels.

Overview



In the first phase of the performance measurement process, you decide which aspects of your group's performance you want to measure. You define your **objectives**, **critical success factors** (**CSF**s), and **performance metrics.**

If your company uses a formal performance measurement (PM) system, one or more of these elements may already be defined for your group by senior managers in the organization or by the unit supervising the performance measurement system. The performance data you gather must then be in a form that's compatible with the companywide system.

If your organization does not have a formal PM system and you want to track performance on important business activities, you'll need to generate your own objectives, CSFs, and metrics.

Key Idea: Define your objectives

Key Idea

Your objectives represent what you want to accomplish in order to improve various aspects of your group's performance. To brainstorm ideas for objectives, meet with colleagues and direct reports in your group and ask the following questions:

- **What does our group hope to accomplish by measuring performance?**

  For instance, does your group hope to identify solutions to recurring problems? Improve overall process efficiency? Determine rewards for particular levels of employee performance?

- **What must our group do to help carry out our company's strategy?**

For example, if your company's strategy centers on operational excellence (improving efficiency), you might set objectives for your group such as "Increase sales revenue per employee," "Lower indirect costs," or "Reduce workplace accidents."

- **How might we better serve our customers?** Whether your group serves internal or external customers, think about how you can provide them with greater value.

  For instance, if you lead an HR group, your objectives might include "Develop future leaders in the organization," "Help managers retain talented employees," and "Foster a collaborative culture." If you lead a product development group, your objectives might include "Increase innovation," "Update products more frequently," and "Make products easier to use."

- **How might we improve our work processes?** Sometimes process problems can be translated into ideas for objectives.

  For example, suppose you lead a group in the accounting department and your direct reports tend to have difficulty meeting deadlines. In this case, you might define objectives such as "Complete accounts receivable reports on time," "Pay vendors according to their terms," and "Process employee expense reimbursements on schedule."

- **What new skills or knowledge do we need to excel?** Objectives for improving your employees' skills and knowledge might include "Take advantage of more training opportunities," "Improve knowledge sharing," and so forth.

After brainstorming ideas for objectives, review your list and identify the most important ones—those objectives that most directly affect company and unit strategy or that will help you solve serious performance problems. Try to whittle your list down to a manageable five or seven objectives.

Defining clear objectives is the first step in measuring performance.

Leadership Insight: Driven by a purpose

When you think about goals, it is very important to think about purpose. What is the purpose of the organization? What larger social objective does the organization achieve? I will illustrate this using the example of Novartis, a large Swiss pharmaceutical company that has been engaged in the development of medicines over many decades.

Daniel Vasella, the chief executive officer of Novartis, felt that the most important purpose of Novartis was to serve its patients. In deciding on goals, Vasella decided that he would identify two that he believed were of utmost importance: meeting unmet medical needs that patients have (that is, developing medicines for diseases for which no medicines existed) and understanding the science of action (the mechanism of action by which these drugs act so that patient needs would really be met).

In developing these medicines and in developing these drugs, Novartis's innovation pipeline, its R&D, and its goals for its innovation pipeline are focused heavily on unmet medical needs.

For example, Novartis produced a drug called Gleevec, which is a medicine that meets unmet patient needs in an area called chronic myelogenous leukemia, which only affects 50, 000 patients. But over a period of time, Novartis has realized that a drug like that keeps on giving.

Novartis uses both financial and nonfinancial measures in setting its goals. This is to meet both the short-term goals that Novartis has as well as the long-term goals. In short-term goals, Novartis uses financial measures such as profits and sales. In long-term goals, Novartis uses measures such as the number of patients for which unmet medical needs have been met, the market share that it has achieved in those markets, the number of new products that it has developed, and the satisfaction and engagement of its people.

At Novartis, goal setting tied to purpose has led to both tremendous benefits for the patients and for its shareholders. As they say, "A good drug keeps on giving."

Goals that align with an organization's purpose—drive results.

Srikant Datar
Board Member, Novartis
Professor, Harvard Business School

Srikant Datar is the Arthur Lowes Dickinson Professor of Accounting at Harvard University. Srikant received the George Leland Bach Award for Excellence in the Classroom at Carnegie Mellon University and the Distinguished Teaching Award at Stanford University.

He is a coauthor of the leading cost accounting textbook "Cost Accounting: A Managerial Emphasis" and of "Rethinking the MBA: Business Education at a Crossroads." Srikant's research interests are in the cost management and management control areas, including activity-based management, quality, and productivity.

His research findings have been published in several prestigious journals, including the Accounting Review, Journal of Accounting and Economics, and Journal of Accounting Research.

Srikant serves on the Board of Directors of Novartis AG, ICF International, KPIT Cummins Info Systems Ltd., Stryker Corporation, and Harvard Business Publishing.

He is a graduate with distinction from the University of Bombay. He received gold medals upon graduation from the Indian Institute of Management, Ahmedabad, and the Institute of Cost and Works Accountants of India. A chartered accountant, he holds two master's degrees and a Doctor of Philosophy from Stanford University.

Key Idea: Define critical success factors

> “Measure what you want, not want what you can measure.”

–Robert S. Kaplan and David P. Norton

For each objective in your final list, decide which two or three actions would best enable your group to accomplish that objective. These become your critical success factors (CSFs). The following table shows examples.

Example Critical Success Factors

Objective	Critical Success Factors
"Reduce workplace accidents"	• "Train employees on proper use of equipment" • "Provide appropriate safety equipment and apparel" • "Regularly inspect workshop for compliance with safety rules"
"Improve knowledge sharing"	• "Improve new-hire mentoring" • "Establish rewards for sharing or accepting new ideas"

Define performance metrics

Your performance metrics indicate how you'll determine whether you've carried out the critical success factors you've identified and indicate the kind of data you'll need to gather. You can translate each CSF into one or more metrics, as shown in the following table.

Example Performance Metrics

Critical Success Factor	Performance Metric
"Train employees on proper use of equipment"	• "Number of employees who complete training course with passing grade by end of quarter"
"Establish	• "Number of new ideas

rewards for sharing or accepting new ideas"	adopted across business units" • "Number of best practices posted to company's knowledge management system"

Activity: Match the metric

When you understand how CSFs translate into actual performance metrics, you take a step closer to gathering the data you need. Can you identify the best performance metrics for different critical success factors?

Choose the best performance measure for the Critical Success Factor: Improve customer satisfaction.

- Increase in sales over six months

  Not the best choice. This particular metric would measure something that might be a result of improved customer satisfaction, but is not a specific and direct method of checking performance against the CSF.

- Percentage increase on satisfaction rating in customer surveys

  Correct choice. This metric is a good measure of the CSF. Using data from customer satisfaction surveys is a good way to quantify a subjective success factor such as improving customer satisfaction.

- Decrease in employee turnover

  Not the best choice. This is not an effective measure of the CSF because it is not a metric that identifies performance closely related to improving customer satisfaction.

- Number of new products offered during fiscal year

  Not the best choice. While new products might make for happy customers, this is not a metric that specifically measures something related to customer satisfaction.

Choose the best performance measure for the Critical Success Factor: Improve sales staff performance

- Number of new employees hired

  Not the best choice. This performance metric does not measure something directly related to improving the performance of sales employees.

- Increase in training costs per employee

  Not the best choice. Though this metric could in time result in an increase in sales, it is not a good way to measure the performance of sales staff.

- Decrease in product failure rate

Not the best choice. Though this metric could in time cause an increase in sales, it is not a good way of measuring the performance of sales staff.

- Percentage increase in number of sales to new clients

  Correct choice. The percentage change in sales to new customers is an easily quantifiable metric that could be derived directly from the CSF of improving the performance of sales staff.

Choose the best performance measure for the Critical Success Factor: Train employees in new production process

- Percentage decrease in product flaws

  Not the best choice. Although successful training could result in fewer product flaws, this metric does not by itself measure success at training new employees.

- Percentage of employees with passing grade on new process evaluation

  Correct choice. The percentage of employees with passing grades is an excellent quantitative metric for measuring the success of employee training.

- Increase in advertising expenditures

  Not the best choice. Measuring new advertising expenditures is not an effective performance metric for training new employees.

- Increase in overall revenue

  Not the best choice. While overall revenue may increase as a result of new process training, it is not specific enough to be an effective metric for this CSF.

Consider the source

In defining metrics, the kind of data you'll need and the sources of data you'll use become important considerations. Ask yourself:

- **Where will you get the needed data?** In some cases, your organization may already collect data that you can use—such as employee participation in certain training programs. In other cases, you'll need to gather the data yourself, which may require you to set up new processes and systems. Data may also come from external sources.

  For example, your company may have hired a vendor to track the number of employees enrolled in benefits programs.

- **How will you gather subjective data?** Performance metrics can require objective *or* subjective data.

  For example, to track the metric "Percentage increase in sales revenue," you'd gather objective data (changes in sales revenue over a specific period of time).

But how would you collect information to track the metric "Percentage increase in customer satisfaction"? In this case, you'd need to gather *subjective* data—such as comments or ratings from customer surveys. Even subjective data must be quantified.

For example, expressing customer satisfaction ratings on a scale of 1 to 5—to enable comparison and highlight opportunities for improvement.

- **Should you use composite data?** If you want a big-picture view of your group's performance, consider using metrics that require composite data—data from numerous sources aggregated into one number. Well-known examples include the S&P 500 stock market index and the J.D. Power index of customer satisfaction with new cars and ratings of new-car quality.

  An example of composite data a company might use to measure performance would be a "brand index," which might combine, say, advertising budget, percentage of target audience reached, and brand impression (what people think of the company's brand, measured in a survey). Because the component measures are dissimilar, they would need to be mathematically adjusted to weight them properly.

- **Will your data be reliable?** While defining metrics, do everything you can to ensure the reliability of the data you'll need to gather.

  For example, will the data be up to date? Sufficiently detailed? Accurate? Auditable? Will the data be available frequently enough for you to reliably track performance on your metrics?

Set targets

In the second phase of the performance measurement process, you gather and check the reliability of data on the metrics you've identified. Start this phase by setting targets for each metric you've defined.

Targets represent the performance you want to see on each of your metrics. The table below shows examples.

Example Targets

Performance Metric	Target
"Number of employees who complete training course with passing grade by end of quarter"	"All employees complete training course with an end-of-course test score of 80 or above out of a possible 100 by end of quarter"

"Percentage of existing products updated with new features midway through the fiscal year"	"85% of existing products updated"
"Customer satisfaction index"	"Achieve 85% of customers that are very satisfied or extremely satisfied, which represents a 15% increase in customer satisfaction by year end"

The art of realistic targets

Setting targets is a bit of an art. For example, you want to set targets that inspire people to deliver exceptional performance. But you don't want to set targets so high that your direct reports assume they can't reach them—and so don't bother trying. In addition, you have to figure out what constitutes reasonable targets.

> For instance, if you're aiming for a defect rate of 100 parts per million (PPM) in a process your group performs, but industry defect rates for a similar process currently range from 400 to 1,000 PPM, your target may be unrealistic.

Leadership Insight: Take risks

I think the important thing to remember about when you're setting goals for your organization is the old adage, "What gets measured gets done." All too often you get caught into really setting or selecting goals that are easily measurable but don't really drive that organization's strategy.

I'm in an R&D organization, and innovation is very important to us. But the challenge is the idea that somehow you can't schedule innovation. Really what I work with our teams on is: we expect them to have failures. That's part of the process. If we had 100% success rate, then we aren't taking enough risks.

And you really have got to make sure that you're going to set up your goals, that they are enabling of that, and that you're not setting goals that cause people not to want to want to take those risks that are really essential to be innovative.

I coach baseball for my son's team. It's a bunch of little leaguers. They definitely are not the best team out there, but we certainly are very competitive. And I think the thing that I'm always working with them on is to understand if the ball gets hit to them, what are they going to do with the ball?

It's not so much that they make the play, but they didn't freeze when they fielded the ball. That's what we celebrate afterwards.

Drawing it back to business, I think there are good parallels to that in that the reason why we set goals is so we can be aware of when we're making progress, aware of if a particular situation comes up, how we might be able to react to it.

If we didn't have plans, if we didn't set challenges and goals, we would spend a lot of time just standing there, holding the ball in our glove, trying to decide what to do next as opposed to making that play.

Set goals that inspire action and help drive innovation.

Dan Groneck
Director, Technology Planning and Execution, Boeing

Dan Groneck is Director of Technology Planning and Execution in Boeing Research & Technology (BR&T), where he is responsible for developing and managing the technology strategy. BR&T is the Boeing Company's central research and development organization, with over 3700 engineers.

Dan first joined the organization in 1997, and in 2005 he was named Executive Program Integrator to Bob Krieger, President of Boeing Phantom Works. In this position Dan led special projects, monitored day-to-day operations of the organization, and coordinated executive-level events. In 2007 Dan became Chief Engineer for over 550 engineers in the AeroStructures, Manufacturing & Support Technology organization within BR&T. He was promoted to his current position in 2010.

Dan holds a bachelor's degree in mechanical engineering and history from Rice University, as well as a Master of Science in mechanical engineering and a Master of Business Administration from Washington University. He attended Harvard Business School's General Management Program. Dan has taught Operations and Project Management at Maryville University and several courses at the Boeing Leadership Center.

Use benchmarking

How do you deal with such challenges while setting targets? Benchmarking can help.

Use information from trade associations, industry publications, the Internet, and outside sources to **benchmark**, or compare your performance data and metrics with those of other companies. Some are very well known—such as the J.D. Power rankings. Also consider internal benchmarking sources—such as performance data from other groups that carry out similar processes or that have similar goals as yours. Then set targets that seem reasonable in light of the benchmarking information you've gathered.

Establish a baseline

If you're setting targets for a performance metric on which your group or company has already gathered actual data, it can be helpful to use that data to establish a **baseline**, or starting point, for your target. Many managers use the current period's results or a yearly average to set their targets.

> For example, if your group's sales have increased an average of 5% every quarter over the past two years, you might consider setting a target sales increase of 6% or 8% per quarter for the coming year.

For metrics on which no data exist, you might research an industry average and use that as your baseline.

Using past data to set a baseline for your targets can be tricky. After all, how do you decide which number should serve as your reference point?

> For example, suppose you want to use sales from the fourth quarter of last year as your baseline. How confident can you be that the fourth-quarter figure represents a useful average of your group's performance? If there were unusual circumstances during that quarter (such as a large number of unfilled sales positions), the figure may not be a good reference point—because sales would be lower than usual.

For these reasons, it's important to carefully evaluate the historical data you're considering using as your target baseline. Look at how the data for a particular period compare with the data from preceding evaluation periods, to see whether there has been an abrupt change from the previous performance. If there has been, you'll want to investigate the reasons for the change by asking your boss and peer managers for insights. And you may want to consider using a different period's data to inform your target.

Determine a target range

Many managers set a three-point (minimum, moderate, and "stretch") range for certain targets.

> For example, for the performance metric "Increase sales," the minimum target might be "$500,000 sales per quarter"; the moderate target, "$800,000 sales per quarter"; the "stretch" target, "$1 million sales per quarter."

This approach offers several advantages. Minimum targets can feel more manageable to employees and help them see what progress they need to make in order to reach the moderate and stretch goals. Though minimum targets aren't truly subpar, managers don't want employees to stop at achieving these targets. The "real" goal is usually the moderate point in the target range.

The "stretch" point in a target range represents the most ambitious target of all. In determining stretch targets, you need to achieve the delicate balance between challenging your employees and being realistic. A stretch target is intended to "raise the bar" enough to get your employees' competitive juices flowing or to stoke their desire for achievement. And it usually requires significant effort to achieve. But it also must be set at a level at which your direct reports have the skills, knowledge, and company resources (equipment, processes, workspace, time) required to meet the target.

To set stretch targets, make sure you're familiar with your employees' capacities and abilities. How have they reacted in the past when presented with ambitious challenges? Ask yourself how much of a stretch will motivate them to outdo themselves without becoming overwhelmed or demoralized. Also consider whether stretch targets carry the risk of encouraging negative or unethical behavior, such as "gaming" the system to achieve the desired performance.

Finally, show your employees how achieving the stretch target on one metric will lead to outstanding performance on another and generate valuable rewards.

> For example, "If we increase customer loyalty 10%, that will translate into a 15% jump in profitability. And that means a boost in your bonus compensation."

Activity: Set the right targets

Setting performance targets is a bit of an art. Choose target-setting strategies that could help inspire employees—without overwhelming them.

A manager wants to set an inspiring target for her group's safety record. She notes that the number of safety incidents in her group decreased an average of 2% each quarter over the past several years. So she sets a target that calls for the number of safety incidents to decrease 7% to 8% per quarter for the coming year.

What mistake has she made?

- She failed to establish a baseline, or starting point, for her target.

  Not the best choice. This manager actually *did* set a baseline, by examining the changes in performance on safety incidents in her group over the past few years.

- The manager did not define a target range for her employees.

  Not the best choice. This manager actually *did* define a target range for her employees—a decrease in safety incidents of 7%-8% per quarter for the coming year.

- The target is too ambitious compared to the group's historical performance.

  Correct choice. Achieving a decrease in safety incidents of 7%-8% (compared to the historical 2%) is asking too much of this team. When a manager sets overly ambitious targets, employees may conclude that they can't reach them—and so they don't bother trying.

To set realistic targets for your team's sales performance, you decide to benchmark. Which of the following steps would not be part of your benchmarking strategy?

- Comparing your team's sales achievements against those of other companies in your industry

  Not the best choice. This actually *would* likely be part of your benchmarking strategy.

- Reviewing your team's sales from the previous year, then setting a target that improves on the historical figures

  Correct choice. This does *not* constitute part of a benchmarking strategy. Instead, it is something you would do to establish a baseline, or starting point, for your sales target.

- Finding out how other sales teams in your organization have performed

  Not the best choice. This actually *would* likely be part of your benchmarking strategy.

A manager wants to establish a minimum, moderate, and stretch target for his group's performance on a quality control metric. What would you advise him to do to get the best performance on these targets from his employees?

- Ensure that the stretch target requires slightly more effort to achieve than the moderate or minimum targets

  Not the best choice. To be effective, stretch targets should actually require significant, not slightly more, effort to achieve than the moderate or minimum targets in the specified range.

- Let employees know that the "real" goal is the minimum target, so that the moderate and stretch targets will seem more manageable

  Not the best choice. In setting minimum, moderate, and stretch targets, it's the moderate point in the range—not the minimum point—that is usually considered the "real" goal. Identifying the minimum point as the "real" goal won't likely motivate employees to strive for performance beyond that point.

- Explain to employees how improving product quality will reduce returns, thereby saving money and making more funds available for the company's profit-sharing program

  Correct choice. By showing employees how achieving a stretch target on one metric will lead to good performance on another—and generate valuable rewards for employees—managers can inspire their people to strive for the stretch target.

Collect data

> “How'm I doing?”
> –Ed Koch, former Mayor of New York City

After setting targets, you and/or your direct reports need to begin gathering performance data so you can compare actual performance with your target performance. Data can come from a number of sources.

For instance, you may ask people in your department who lead call center teams to track the number of phone calls customers must make before representatives resolve their complaints or questions.

You may also depend on people in other groups or units to gather data on your performance metrics. Many companies identify "metric owners," who have specific knowledge that enables them to collect valid data on a performance metric.

To illustrate, perhaps someone in the HR department will supply data on the number of employees in your group who have attended safety-training courses and passed the end-of-course test. Or, the finance manager can give you interim profitability numbers.

If your company has a formal performance measurement system in place, senior managers or a dedicated unit may have created data-gathering forms for you and other managers to use. These may be hard-copy documents—such as memos that you fill in by hand and submit to a PM system administrator. Or they may consist of electronic forms—spreadsheets or Web-based data entry forms that you fill in online and e-mail to the PM system administrator.

Communicate data

Automated data-gathering systems, often linked to a company's data warehouse or enterprise resource planning system, offer numerous benefits. They handle huge volumes of data easily and can generate reports showing the data in different formats (such as pie charts, tables, or graphs). In addition, they can aggregate data from different units or groups into one number.

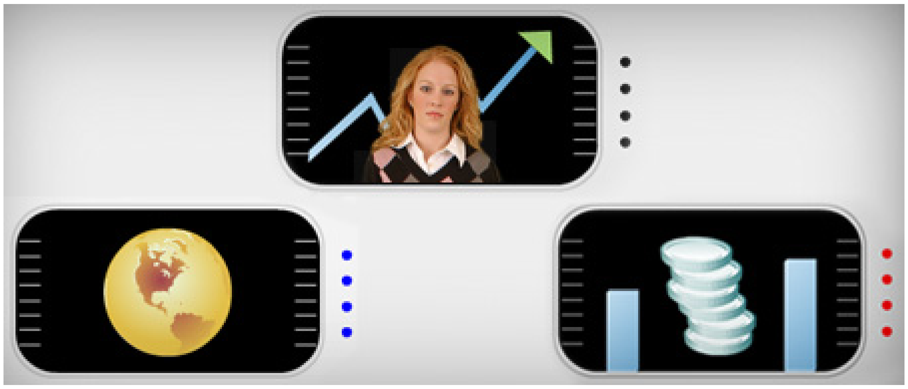
> For instance, the system may show "Division sales," while also enabling managers to drill down to see sales generated by each region and salesperson within the division.

They also help you analyze cause and effect by enabling you to "slice and dice" data in different ways.

If your organization doesn't use a formal performance measurement system, you may need to develop data-gathering forms yourself. In this case, simplicity and ease of use are critical to getting the data you need. Develop a consistent form that enables you and other metric owners to provide information easily, conveniently, and quickly, and that accommodates short notes regarding the data. Below is an example of a simple, easy-to-use data-gathering form for the metric "Percentage of one-call resolutions":

Metric	Target	Performance Data			Notes
"Percentage of one-call resolutions"	75% per month	July 55%	Aug. 65%	Sept. 55%	September data is misleading. The percentage of one-call resolutions logged that month fell far short of the target—but that's because during the peak summer vacation period, we were short-staffed and had to hire temps who were less knowledgeable.

Analyze data



In the next phase of the performance measurement process, you analyze the data you've gathered on your performance metrics and determine their implications. Interpreting performance data is a complex discipline in itself. In many companies, this activity is performed by a unit staffed by experts trained in statistical analysis, correlation and regression analysis, and other data-interpretation approaches and tools.

But in the interest of gaining an overview of the entire performance measurement process, it's helpful to know a bit about how performance data are evaluated and what you and others might look for when interpreting results.

Compare actual performance with targeted performance

You've been gathering data on your performance metrics for some time. What should you do with the data? What do the numbers mean? A good first step is to compare your data with the targets you set for each metric.

> For example, suppose you set the target "5% maximum product manufacturing error rate," to be reached at the end of six months.
>
> You've tracked *actual* error rates over the past six months, and recorded the following rates:
>
> Clearly, the error rate has fluctuated over the period in question, with a general downward trend. And the rate at the end of the six months is not as low as the 5% you set as your target. How should you respond? You might draw several conclusions:

1. "We didn't reach our target, so we should overhaul our error-reduction efforts. Perhaps we need a new initiative focused on sharpening shop-floor staff training in using the manufacturing equipment."
2. "The trend is generally downward. Even if we didn't reach our target by the end of the six months, we seem to be heading in the right direction. Let's see what happens over the next few months, and decide whether we need to reexamine our error-reduction efforts."
3. "The target was too aggressive. We don't have the capacity to reduce errors as much as we had hoped. Let's revise the target to make it less aggressive—say, a 9% error rate."
4. "Perhaps the data aren't reliable. How do we know we can trust these rates?"

Given all these possible interpretations, how do you select the best response to what you're seeing in your data? Savvy managers keep a number of guidelines in mind.

Guidelines for interpreting performance data

Consider the following four practices for deciding how to respond to your performance data:

- **Looking for trends** can help you identify the bigger picture of how performance is changing over time, as reflected in the data you're gathering. If your actual performance is trending in the desired direction, you may not need to intervene.
- **Considering the inherent variability in the process being measured** will help you keep perspective. You don't want to overreact to a variation in performance measures that is due to normal fluctuations.

    For example, sales on a particular line of products may vary across seasons. Some companies set ranges of normal variation for such metrics and respond only when actual performance is outside that range.

- **Thinking about what's causing any variations in the data** will help explain the causes beneath variations**.** Ask yourself what events or forces might underlie the variations you're seeing in your performance data.

    For instance, suppose you see a major jump in error rates during month 3 of your data-tracking period. You'd want to investigate what was going on during that time that might have affected the error rate. Was a new piece of manufacturing equipment introduced at that time, and did the production staff have difficulty using it? Maybe the shop floor took on several new hires that month, and they hadn't yet mastered use of the equipment. In each of these cases, you might decide to hold off taking drastic action.

- **Asking whether your targets or metrics need to be changed** will help you determine if you need to reconsider your targets or metrics. Sometimes, when you see an abrupt change in your performance data, it's a signal that you need to reconsider your targets or metrics. Such signals can occur if your organization has changed an important process. An abrupt change in error rate may, for example, result from an employee scheduling change. Perhaps after starting your measurement program, you stopped the practice of allowing employees to vary their shifts, assigning each person a permanent shift. That could cause error rates to drop and then stabilize—suggesting that you can reasonably set lower targets for that metric.

    Here's another example. Suppose that over the past 12 months, you've been tracking the number of weeks it takes to fill vacant positions in your group, with the goal of bringing new hires on board faster. At month 6, the number of weeks decreases sharply—and stays at roughly the same level during months 7 through 12.

    When you investigate, you discover that your company's HR department overhauled its recruiting processes during month 6—by installing an online job-posting and job-application module in its human resource information system (HRIS). This new technology has vastly accelerated the hiring process—so that many new hires can now take days instead of weeks.

    Suddenly, your metric "Number of weeks" has less meaning than it did before. If you still want to accelerate the hiring process, you might change your metric to "Number of days." Or, you may decide that the new technology has helped you improve the hiring

process sufficiently—and you now want to measure some other aspect of your group's performance.

Clearly, interpreting performance data can be complex and challenging. Your company may have a unit devoted to analyzing all performance data. If it doesn't, and if you're struggling to make sense of a particular set of data, seek help from your boss or from an expert in your company who specializes in statistical analysis.

Confusion over number of metrics

Managers who measure performance routinely encounter common pitfalls during each phase of the process. To avoid these pitfalls, start by understanding them.

Avoid relying on just one metric to measure your group's overall performance. Also resist any urge to create a long list of metrics to measure everything you can think of that relates to your group's performance. The goal is to identify the activities that will have the greatest direct impact on your group's performance—and develop metrics for those activities.

If you've defined three or four major objectives for your group, each of those will likely be translated into two or three critical success factors. Each CSF, in turn, will be translated into one or more performance metrics. Thus, four objectives may ultimately translate into as many as 24 metrics. If the number of metrics grows much larger than this, you'll expend too much energy tracking data and will lose the "big picture."

Unaligned metrics

Ensure that the objectives and metrics you define support your company's and unit's strategic goals. Too many managers decide to measure aspects of their group's performance that have little connection to higher-level goals.

> For example, a call-center manager might take a keen interest in his group's ability to process customer phone calls quickly. The manager tells his employees that he's measuring how quickly they process and complete calls—and bases their performance evaluations on this metric. You can be certain that employees will work hard to get callers off the line promptly. But if the company has defined a strategy involving cross-selling, hustling callers off the phone as fast as possible could easily undermine the corporate strategy.

Overly aggressive targets

It's tempting to think that setting aggressive "stretch" targets for your metrics will get your employees' competitive juices flowing and generate unprecedented performance. While that's a possibility, aggressive targets can also demoralize your employees if they lack the resources to meet the targets and if they view the targets as unreachable and unrealistic. You want to set targets high enough to inspire your direct reports to reach for better performance—but not so high that employees conclude they can't possibly reach them.

Setting overly aggressive targets can backfire in another way—by motivating unethical, possibly even illegal, behavior.

> For example, tough sales and revenue targets have led to serious problems in the insurance industry, resulting in a federal investigation of company practices.

Risk of manipulation of performance data

A company's or unit's selection of metrics can sometimes lead managers to "game" the system so as to meet the targeted performance.

> For example, consider a car company that aims to be "the best-rated customer service car company in the industry." This company will have metrics related to customer satisfaction, customer loyalty, and the number of customer complaints.
>
> New-car salespeople who work in this company know that their compensation depends on what customers write in the feedback forms that corporate headquarters sends them after a sale. Immediately upon closing a deal, salespeople may "coach" the customer on how to fill out the form. They may even appeal to the customer's compassion: "My income depends on what you say on the form. I hope you'll help me." Result? Annoyed customers who feel manipulated by desperate salespeople—and a lack of valid feedback to the company about its salespeople's performance.

Here are additional examples:

> Your direct reports (or even your peers in other departments) may purposely low-ball targets so they can easily exceed them and get bonus compensation and recognition. Or a sales team leader may exaggerate the tough selling environment so you'll set low sales targets and he can look like a star performer without having to work too hard.

The lesson here is that measurement systems can change employees' behaviors—sometimes in ways a company never intended! Avoid this scenario in your own group by making sure to do the following before you set targets:

- Take time to find out how your people might be altering their behaviors in order to meet targets you've set for the performance metrics you're using.
- Consider whether these behavior changes might be causing unintended—and unwanted—consequences for your group and your company.
- If you ask some of your direct reports to provide input on target setting, try to verify the rationale behind their suggestions. Don't just take them at their word; ask them what sources they're using to form their opinions about targets, and verify the reliability of those sources.

Difficulty validating your data

Validating data means assessing their accuracy and reliability. Some data—such as revenues or expenses—are easily validated because they're objective and regularly audited.

> For example, you can tabulate invoices generated by your group to determine whether the revenue figures for your group are correct. Or you can review accounts payable figures to judge the accuracy of expense information.

Data provided by outside sources—such as organizations that track companies' market share—can also be considered valid.

Other data are more difficult to validate. Consider employee morale, a new product's innovativeness, and customer satisfaction. Such things may be important indicators of your group's performance. But how reliable are the data you gather on these metrics? Because such data are subjective, they can be easily manipulated by individuals seeking to make their performance look better than it really is. Still, subjective data are important. In fact, leading indicators are often predominantly subjective (customer surveys and employee morale, for example), and are valuable because they can help your organization proactively manage performance. However, avoid relying on just one subjective metric as the indicator for a critical success factor. A single subjective metric won't give you a comprehensive enough picture of what's going on.

Inappropriate responses to performance shortfalls

When you see actual performance data that falls far short of your target performance, avoid the following inappropriate responses:

- **Knee-jerk interventions.** Don't overreact to every performance shortfall. You might intervene too quickly—such as by firing someone, or launching a large-scale, expensive change initiative that doesn't address the real reasons behind the shortfall. Instead, take time to investigate what may have caused the performance shortfall and to consider a range of possible solutions to the problem.
- **Lowering your targets.** The simplest way to close gaps between targeted and actual performance is to lower your targets so they're easier to reach next time around. But that approach misses the point of performance measurement. Sometimes a target may in fact be too aggressive and merit revision. But in other cases, the more appropriate response is to identify reasonable changes in processes, organizational structures, and other aspects of your group to bring actual performance up to targeted performance.

Failure to regularly reassess your objectives and measures

Things change. The economy shifts. New competitors emerge. Your company or unit modifies its strategy. Your customer base changes. Technology advances. What was significant to your company's success three years ago may no longer be significant today.

Your performance objectives and metrics need to be relevant to current business conditions, yet you also want to keep metrics as consistent as possible over time so you can compare historical performance. The solution? Regularly assess changes in your external and internal environment. And strive to maintain a balance: Keep objectives and metrics consistent where possible and appropriate, modifying them only if necessary to reflect changing realities.

Avoiding the pitfalls described above is critical to accurately measuring your group's performance. When you collect data that truly reflect what's going on in your group, you can more effectively *manage* your own and your employees' performance.

Activity: Avoid performance measurement pitfalls

Mistakes in measuring business performance can lead to unpleasant consequences. Learn to recognize the most common pitfalls, so you can plan to avoid them.

Mario is trying to figure out where he and his underperforming team went wrong.

Mario has found that he and his team are spending much more time and energy than they expected tracking data on their performance metrics. Which performance measurement pitfall might Mario and his team fallen into?

- Failing to regularly assess the team's performance objectives and metrics

  Not the best choice. This pitfall would not likely cause the problems that Mario and his team are experiencing. Instead, failing to regularly assess a team's objectives and metrics could cause a team to have outdated metrics that no longer reflect changes in business conditions, such as new competitors or new company strategies.

- Defining too many major objectives for the team

  Correct choice. Mario may have defined to many major objectives for his team. Typically, each objective has two or three critical success factors, each of which translates into one or more performance metrics. Thus, an overabundance of objectives can create so many metrics that managers end up expending too much energy tracking data on those metrics.

- Using too few metrics that call for subjective data

  Not the best choice. This pitfall would not likely cause the problems that Mario and his team are experiencing. Instead, using too few metrics that call for subjective data (such as employee morale or customer satisfaction) could cause a team to have a shortage of leading indicators. And without sufficient leading indicators, managers can't proactively manage their team's performance.

Bella has begun noticing that the customer feedback her team members are collecting during after-sales phone surveys is uniformly positive overall. Bella is concerned that this feedback may

not be genuine or valid. Which performance measurement pitfall might Bella and her team fallen into?

- Defining objectives and metrics that don't support the company's or unit's strategy

  Not the best choice. This pitfall would not likely cause the phenomenon that Bella and her team are seeing. Rather, defining objectives and metrics that don't support strategy could lead to undesirable (and unexpected) business outcomes. For instance, a company fails to achieve its cross-selling goals because call-center employees are being told to process customer phone calls more quickly than before.

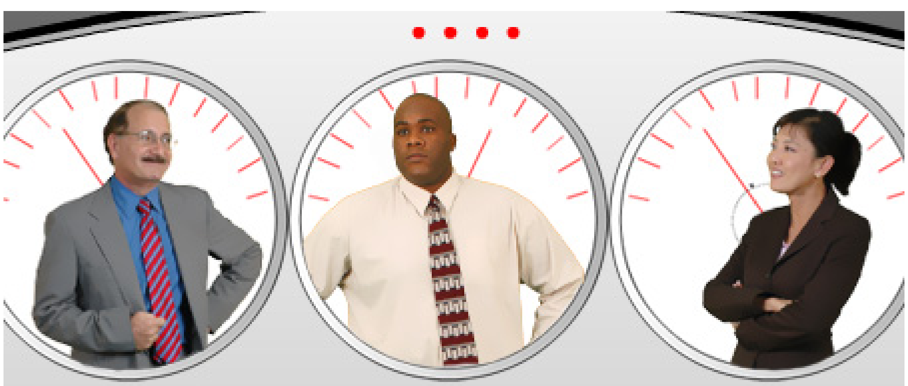
- Overreacting to performance shortfalls by launching major change initiatives

  Not the best choice. This pitfall would not likely cause the phenomenon that Bella and her team are seeing. Instead, responding to performance shortfalls by launching major change initiatives would likely cause a team to notice that, despite extensive investments in change, performance shortfalls persist.

- Selecting metrics that lead employees to manipulate performance data

  Correct choice. Uniformly positive feedback suggests that the performance data may not be objective. For example, salespeople may be "coaching" new customers to give positive responses to after-sales survey questions so that the salespeople meet targets related to customer satisfaction—and earn bonuses.

Manage performance



By *measuring* your group's performance, you ultimately *manage* that performance more effectively. In other words, by pulling away from your daily routine and thinking carefully about how your group does what it does, you can determine how effectively your group is operating. You can then address shortfalls and other problems—whether they stem from your direct reports' performance, your managing style, or some other source.

Consider the following story about Maura, who heads up a large sales group. Through the process of measuring her group's performance, she makes some insightful discoveries that help her manage her group more effectively.

Set objectives, critical success factors, and metrics

Maura was recently promoted to manager of a large sales group. Her company does not use a formal performance management system, so she and her boss work together to define objectives for her group. Since the company has defined a strategy for enhancing profitability and market share, Maura and her boss select several objectives—including increasing customer satisfaction, improving sales staff morale, and boosting sales revenues—that support those high-level goals.

Maura also defines critical success factors for each of her group's objectives.

> For example, her CSFs for increasing customer satisfaction include "Reduce sales staff turnover," "Improve sales staff responsiveness," and "Reduce order-processing errors."

For many of Maura's objectives, reducing sales staff turnover is a CSF. As Maura explains to her boss:

- If turnover increases, customers become uneasy because the sales reps they've come to know are no longer available to them. Worried customers may start taking their business elsewhere.
- Turnover also affects morale among sales reps who remain with the company. If more sales staff start leaving, those who remain may start asking themselves why so many of their former colleagues have defected. They may decide to leave as well—further worsening turnover.
- Turnover burdens remaining reps with larger workloads, because it takes time to hire new reps to replace the defectors. Struggling under heavy loads, remaining reps may have difficulty closing deals—thus reducing the company's revenues.

After defining CSFs for each of her objectives, Maura translates them into metrics. For instance, her metric for sales staff turnover is "Percentage annual turnover in sales staff." Other metrics include "Revenue per sales staff," "Number of order-processing errors," "Customer loyalty," and "Number of calls required to resolve customer complaints and questions."

Gather performance data

Maura next sets targets for each of the metrics she has defined. She and her boss think carefully about the targets.

> For example, Maura knows that she can't eliminate turnover entirely in her group. But she wants to keep it at a minimum. She benchmarks sales staff turnover in other, similar companies, as well as in other customer-facing groups within her organization. After reviewing the information, she decides that a target of 5% annual turnover is reasonable and will help her achieve her objectives. She uses a similar process to set targets for her remaining metrics.

Maura then begins gathering performance data on all the metrics she has defined, and compares the data to her targets.

> For instance, she starts tracking the number of sales reps who leave the company each month and calculating how that rate compares with the 5% annual turnover rate she had set as her target. She figures her target is a monthly average rate of 0.4% (0.4% x 12 = 5% annual).

In gathering and reviewing performance data, Maura sees some disturbing developments. In particular, turnover in her group is trending upward. Over the six months that Maura has been measuring performance, monthly turnover rates have slowly climbed from 0.4% to 0.5%. Turnover for the current month has already reached 0.7%—and there are still two weeks remaining in the month.

In addition, increasing turnover has clearly begun to hurt customer satisfaction and revenues—just as Maura had feared. Performance on the metrics she defined for those objectives has fallen far short of

the targets she set.

Maura knows she must investigate and address the causes behind these performance shortfalls.

Interpret performance data

Maura sets out to interpret the performance data she's seeing—to determine what it's telling her and how she might intervene.

> For example, to investigate increasing turnover rates, Maura takes the following steps:

- **She looks for trends.** For instance, she asks herself whether sales rep departures demonstrate any patterns—such as increasing sharply just after quarterly bonuses are paid.
- **She considers historical context.** Maura asks the HR department what the turnover rates have been in her group for the several years before she came on board.
- **She identifies underlying themes in the reasons behind defections.** For example, do most of the sales reps who leave go to work for a particular competitor? Are many of them making career changes? Have they expressed dissatisfaction with certain aspects of the company or her leadership? Has the company announced plans for a merger or acquisition, or plans to discontinue a product line that might mean sales force layoffs?
- **She compares her group's turnover to that of other groups.** For instance, are other customer-facing groups experiencing similar turnover rates? What about industry averages?

Painful – but productive – discoveries

Through this process, Maura makes several discoveries. For one thing, she finds that her group has been experiencing higher turnover rates than other customer-facing groups in the company. She also determines that turnover has increased steadily since she began leading the group. Equally troubling, she learns that departing sales reps' exit interviews contain a preponderance of comments about her "unavailability."

As painful as these realizations are, they enable Maura to design and implement solutions to the turnover problem.

> For example, she begins holding more frequent meetings with sales reps and getting to know more about their career interests. She also has lunch with several peer managers and asks them how they control turnover in their sales groups. She adopts some of their suggestions. These include responding more quickly to phone calls and e-mails from sales reps who need help resolving problems or who want to explore ideas for better serving customers.

Maura's efforts pay off: Over the next two quarters, turnover in her group levels off. During the following quarter, it even begins to decline. Customer satisfaction rates start improving, and revenues for her group begin to pick up.

By *measuring* her group's performance, Maura has discovered how to better *manage* that performance. As a result, she has begun generating more value for her company and its customers—and is helping her organization achieve its strategic goals.

Key Terms

Balanced Scorecard. A performance measurement system that assumes that financial performance is just one part of the larger picture of organizational performance. The system seeks to balance a company's financial perspective with three additional perspectives: customer, internal processes, and workforce learning and development. See also *performance measurement system*.

Baldrige National Quality Program. A quality-improvement performance measurement system that defines criteria for high-quality business performance in areas such as leadership, strategic planning, customer focus, and knowledge management. The Malcolm Baldrige Award, along with its European equivalent, is a prestigious annual award that recognizes organizations for achievement in specific categories: manufacturing, small business, education, and health care. See also *performance measurement system*.

Benchmarking. Using information from trade associations, industry publications, or the Internet, data from other groups in your company, and information from other sources to compare a group's, unit's, or company's performance data and metrics with those of other business entities. Many managers who use benchmarking do so in order to identify best practices that they want their group to emulate. Benchmarking is also helpful for creating performance metrics and setting targets. See also *performance metric* and *target*.

Cockpit. See *dashboard*.

Critical success factor (CSF). The activities a group, unit, or company must carry out to achieve its objectives. See also *objectives*.

Dashboard. A performance measurement system that combines a company's metrics, targets, and performance data into one online or printed document, such as a spreadsheet, that is prepared on a regular basis. Also called cockpit. See also *performance measurement system*.

Data validity. A quality of performance data. Valid data can be checked for their accuracy and reliability. For example, revenue data can be confirmed by tabulating invoices generated.

Economic value added (EVA)™. An output KPI that expresses the value of a business activity that is left over after you subtract from it the cost of executing that activity and the cost of the physical and financial capital deployed to generate the profits. EVA can be expressed as net operating profit after taxes minus net operating assets multiplied by the weighted cost of capital. See also *output KPI*.

External data. Performance results generated outside a company, such as a third-party organization's rankings of companies' performance against competitors'. See also *internal data*.

Financial performance. Business results related to a company's financial health, such as revenues, expenses, and profits. See also *nonfinancial performance*.

Input KPI. A key performance indicator that measures the assets and resources a company has invested in or used to generate business results. Examples include dollars spent on research and development, funding for employee training, and quality of raw materials. See also *key performance indicator*.

Internal data. Performance data generated within a company, such as sales, customer satisfaction, and number of new hires. See also *external data*.

Key performance indicator (KPI). A measure reflecting how an organization is doing in a specific aspect of its performance. A KPI is expressed as a critical success factor—the key determinant of success in achieving any given strategic objective. See also *critical success factor*, *input KPI*, *output KPI*, and *process KPI*.

Lagging indicator. A metric that looks "backward" in time at what a company has already achieved in the past, such as sales. See also *leading indicator*.

Leading indicator. A metric that looks "forward" in time, suggesting the results a company may expect to see in the future. For example, customer-satisfaction ratings suggest how customers may buy from a company in the future. See also *lagging indicator*.

Market share. The percentage of sales in a given industry segment or sub-segment captured by your company. See also *output KPI*.

Metric. See *performance metric*.

Minimum target. The lowest point in a three-point target range that a group, unit, or company sets for a performance metric. See also *target* and *performance metric*.

Moderate target. The midpoint in a three-point target range that a group, unit, or company sets for a performance metric. See also *target* and *performance metric*.

Nonfinancial performance. Business results related to aspects of a company's health other than financial performance, such as employee knowledge, information systems, and customer relationships. See also *financial performance*.

Objective. Goals that a group, unit, or company wants to accomplish in order to improve performance. Objectives may be related to strategy, to customer service, to business processes, and so forth.

Objective data. Performance data that are easy to quantify, such as revenues, expenses, and workforce headcount.

Output KPI. A key performance indicator that measures the financial and nonfinancial results of business activities. Examples include revenues, number of new customers acquired, and percentage increase in full-time employees. See also *key performance indicator*.

Performance measurement system. A set of strategic objectives and performance metrics (including KPIs) applied throughout an entire enterprise.

Performance metric. Indicators of a group's, unit's, or company's ability to carry out the critical activities needed to achieve its objectives. For example, the performance metric for the critical activity "Train employees on proper use of equipment" might be "Number of employees who complete training with passing grade."

Plan-Do-Check-Act. A quality-improvement performance measurement system comprising four steps: (1) Plan: Identify a performance problem and the processes affecting it. (2) Do: Explore potential solutions and implement one. (3) Check: Assess how well your solution worked. (4) Act: If your solution worked well, institutionalize it and look for another improvement opportunity. See also *performance measurement system*.

Process KPI. A key performance indicator that measures the efficiency or productivity of a business process—for example, product-repair cycle time, days to deliver an order, or time to fill vacant positions. See also *key performance indicator*.

Return on investment (ROI). An output KPI that represents the benefits generated from the use of assets in a company, unit, or group, or on a project. ROI is expressed as net income (revenues minus expenses and liabilities, such as taxes) divided by total assets. See also *output KPI*.

Six Sigma. A quality-improvement performance measurement system that stresses the continual improvement of business processes through reduction of errors. See also *performance measurement system*.

Stretch target. The most ambitious point in a three-point target range set by a group, unit, or company for a performance metric. See also *target* and *performance metric*.

Subjective data. Performance data that are difficult to quantify, such as customer satisfaction, employee morale, and product innovativeness. Leading indicators often require subjective data. See also *objective data* and *leading indicator*.

Target. The performance that a group, unit, or company wants to achieve on a performance metric. Targets are often expressed as three-point ranges. For example, for the metric "Percentage of employees who complete training with passing grade," the target may be "80% minimum, 90% moderate, and 100% stretch." See also *minimum target*, *moderate target*, *stretch target*, and *performance metric*.

Trend. Changes in performance data that form a pattern over time. For example, average error rate declines over six months. Managers examine trends to decide how to respond to gaps between target performance and actual performance.

Overview

This section provides interactive exercises so you can practice what you've learned. These exercises are self-checks only; your answers will not be used to evaluate your performance in the topic.

Scenario

Assume the role of a manager in a fictional situation and explore different outcomes based on your choices (5-10 minutes).

Check Your Knowledge

Assess your understanding of key points by completing a 10-question quiz (10 minutes).

Scenario: Part 1

Part 1

Allen leads a product development group in the electronics unit of Hainsworth & Smith, a large consumer goods company. At Hainsworth & Smith, unit managers have traditionally used financial metrics to assess their units' performance. But in the face of heightened global competition, the company has decided to revise its performance measurement system. A more comprehensive system, management believes, will help Hainsworth & Smith fortify its market position.

Top management has asked leaders in each business unit to form a special task force charged with defining new metrics for their unit—metrics that focus on both financial and nonfinancial measures. Allen's boss has asked him to participate in the electronics unit's task force. This task force also includes representatives from other functions within his unit—such as manufacturing,

operations, finance, and IT. All task forces will share their ideas with an executive steering committee, which will then combine the ideas to build the most appropriate companywide performance measurement system.

At the task force's first meeting, the project leader invites everyone to offer ideas for how to begin the revision process.

What's the best suggestion for how the task force might begin its work?

- Immediately benchmark against the performance metrics of similar companies to take advantage of best practices

  Not the best choice.

  Benchmarking against other companies' performance metrics is a positive way to generate some interesting ideas for the task force—but it shouldn't be the first step Allen takes. Each company has different goals and challenges, so one company's metrics may not be appropriate for her organization. The metrics he ultimately chooses need to reflect her unit's unique set of circumstances, aims, and challenges.

- Identify the three or four most crucial processes performed in the unit that will eventually be assigned metrics—such as visiting potential new customers, training employees, and so forth

  Not the best choice.

  Though metrics related to processes are very useful, the purpose of measuring is to help improve results. The task force eventually needs metrics related to outcomes—such as the number of customer visits that generate sales, and the number of trainees who demonstrate that they acquired the right skills during training. But Allen won't engage in this process until he has talked with managers in other units to clarify the company's strategic goals.

- Talk with high-level unit managers to clarify the company's strategic goals

  Correct choice.

  A unit's performance metrics should be linked to the company's strategy. That is, they should indicate how well the unit is supporting execution of the strategy. For example, if Hainsworth & Smith's strategy hinges on being a provider of cutting-edge products, the electronics unit might ultimately define metrics related to product innovation.

Scenario: Part 2

Part 2

Everyone agrees that clarifying Hainsworth & Smith's strategy is an essential first step in the task force's work. Over the coming week, several members of the team meet with managers throughout the unit to obtain their thoughts about what part the unit plays in executing the company's strategy.

When the task force reconvenes, members affirm that Hainsworth & Smith's strategy indeed centers on building a global reputation as a company on the leading edge of technology. Now that the team understands the high-level strategy, members feel prepared to generate ideas for moving their work forward.

What should Allen recommend for moving the task force's work forward?

- Identify the one most important high-level objective that would enable the unit to support the corporate strategy—such as improving product innovation or increasing market share

  Not the best choice.

  Allen shouldn't define just one objective for his unit. He'll need a set of objectives to get the most comprehensive and balanced picture of his unit's performance. Eventually, these objectives will be translated into a blend of metrics that include financial and nonfinancial, internal and external, objective and subjective, and lagging and leading indicators that will enable him to assess how well his unit is achieving its objectives.

- Brainstorm as many aspects of his unit's performance as the task force can think of, to ensure that he generates a metric for every aspect

  Not the best choice.

  Brainstorming as many aspects as possible would distract Allen from something else he should be doing at this stage: identifying objectives for his unit that support the company's high-level strategy.

- Select several strategic objectives for his unit, then define the critical activities necessary for achieving those objectives

  Correct choice.

  The best way to develop metrics is to establish four or five strategic objectives for his unit that support his company's strategy. The electronics unit, for example, might define

objectives including "Boost rate of successful innovations introduced," "Develop more innovative products for mobile use," and "Speed products to market." Next, his task force would define two or three critical success factors (CSFs) for each strategic objective. CSFs are the activities most essential to achieving a particular objective. For instance, a CSF for "Speed products to market" might be "Reduce product cycle time." The task force would then translate each CSF into one or more performance metrics, for example, "Average product cycle time."

Scenario: Part 3

Part 3

After extensive debate, the task force members finally agree on several strategic objectives for the electronics unit. The team defines a few CSFs for each objective and then translates the CSFs into performance metrics. Allen and his fellow team members realize that the final list of 17 metrics probably isn't perfect, and that they'll likely need to revise the list once managers have used the metrics for several months and have ideas for improving or replacing them.

The task force shares its list of metrics with the steering committee, which approves them as a good starting point. The steering committee then challenges the team to suggest the best approach for assessing performance over time, including setting targets for each metric. At the next task force meeting, the group reviews historical data to select baselines, or starting points, for targets. The project leader then invites team members to offer ideas for next steps.

What idea should Allen offer?

- To stimulate employees' competitive spirit, set only aggressive targets that substantially exceed the industry benchmarks the task force will research

  Not the best choice.

  Though "stretch" targets can inspire people to deliver exceptional performance, such targets on their own can demoralize people if they're unrealistic. For example, if industry benchmarks show that product development times typically range from 24 to 27 months, Allen wouldn't want to set a target to launch new products in 12 months. Given the industry's current best practice, employees would likely view a 50% reduction in product launch time as an unrealistic target. Any attempt to reach this target may be marked by discouragement and end in failure.

- To win employees' commitment, set a range of targets for each metric: a moderate improvement over historical trends,

augmented by minimum expected results and aggressive improvement over past performance

Correct choice.

Setting a range of targets can help motivate employees by showing them the gains they need to achieve in order to boost performance dramatically. In a three-point target range, the "moderate" (midpoint) target represents performance that is slightly beyond what the group can achieve by continuing historical trends. It's achievable if people work together and contribute new ideas about how to achieve the moderate point. The moderate target is augmented by two additional targets: a minimum expectation for improvement over current levels, and an aggressive "stretch" target that lies somewhat beyond what now seems achievable. Stretch targets, if achieved, would represent a dramatic improvement in performance in the eyes of customers and other stakeholders.

- To ensure that employees support the targets, agree that managers will lower a target if performance shortfalls suggest that the target was overly ambitious

Not the best choice.

Lowering targets when actual performance falls short of the target is a simple way to close the gap between targeted and actual performance. But this approach misses the point of performance measurement. There will be times that a target will turn out to be too aggressive and unrealistic, and thus merit lowering. But more often, a more appropriate move is to identify and implement reasonable adjustments to processes, systems, and other aspects of a group's activities to bring actual performance up to the desired levels.

Scenario: Conclusion

Conclusion

After some discussion, the task force members agree to set minimum, moderate, and stretch targets for the metrics they've created. The team submits its ideas to the steering committee, which approves them with just a few changes. In particular, the committee suggests revising several targets to improve overall organizational performance. For instance, committee members point out that the revenues from new product introductions must constitute 20% of total revenues—not the 5% target set by the task force—to generate the significant increase in overall market share the company is aiming for.

The steering committee then combines Allen's task force's proposals with those of other units' task forces to develop a companywide performance measurement system. The system is

implemented and revised over the coming year. The following year, Hainsworth & Smith begins to see measurable results in the form of increased share price, a modest boost in market share, new process efficiencies, and improvements in employees' knowledge sharing. Revising the company's approach to performance measurement has required much time and patience—but the effort has begun to pay dividends.

Activity: Check Your Knowledge: Question 1

What is performance measurement?

- Assessing business results to determine a company's effectiveness and to address performance shortfalls and process problems

  Correct choice.

  By measuring performance, companies determine the effectiveness of their strategies and operations and identify solutions to performance shortfalls and other problems. Organizations measure their performance for numerous additional reasons—including determining whether to revise budgets and forecasts, identifying weak areas to gain a competitive edge over rivals, and distributing performance-based incentives and rewards fairly to employees.

- Automating performance data collection and reporting so that managers can more quickly assess their group's effectiveness and identify performance problems

  Not the best choice.

  Though some companies do automate performance data collection and reporting, performance measurement isn't about automation. It's about assessing business results to determine how effective a company's strategies and operations are and to make changes to address performance shortfalls and other problems. Organizations measure their performance for numerous additional reasons—including determining whether to revise budgets and forecasts, identifying weak areas to gain a competitive edge over rivals, and distributing performance-based incentives and rewards fairly to employees.

- Setting ambitious targets for every employee in a group so that people feel motivated to deliver their best performance possible on the job

  Not the best choice.

  Setting targets is just one step in the larger performance measurement process—which entails assessing business results to determine how effective a company's strategies and operations are and to make changes to address performance shortfalls and other problems. Organizations measure their performance for numerous additional reasons—including determining whether to revise budgets and forecasts, identifying weak areas to gain a competitive edge over rivals, and distributing performance-based incentives and rewards fairly to employees.

Check Your Knowledge: Question 2

What is a key performance indicator?

- A measure indicating an individual manager's ability to effectively lead his or her group

  Not the best choice.

  Rather than focusing on individual managers' leadership abilities, key performance indicators (KPIs) are measures reflecting how an organization is doing in specific aspects of its performance. Organizations may have key performance indicators for all their areas of operation, or they may focus their KPIs on only one aspect of their operations. For example, a social service nonprofit might focus its KPIs on the amount of aid granted to different entities that it serves.

  Many organizations use three types of KPIs: *Process* KPIs measure the efficiency or productivity of a business process (such as "Product-repair cycle time"). *Input* KPIs measure assets invested to generate business results (such as "Dollars spent on research and development"). *Output* KPIs measure the results of business activities (such as "Revenues").

- A measure reflecting how an organization is doing in a specific aspect of its performance

  Correct choice.

  A key performance indicator (KPI) is a representation of a critical success factor—the key determinant of success in achieving a strategic objective that a company or unit has defined. Organizations may have key performance indicators for all their areas of operation, or they may focus their KPIs on only one aspect of their operations. For example, a social service nonprofit might focus its KPIs on the amount of aid granted to different entities that it serves.

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- A measure representing a company's overall standing in its industry compared to rivals

  Not the best choice.

  Though a company may have a key performance indicator (KPI) to represent where it stands in terms of revenue or some other criterion compared to rivals, most organizations have a set of KPIs measuring various aspects of their performance. Organizations may have key performance indicators for all their areas of operation, or they may focus their KPIs on only one aspect of their operations. For example, a social service nonprofit might focus its KPIs on the amount of aid granted to different entities that it serves.

  Many organizations use three types of KPIs: *Process* KPIs measure the efficiency or productivity of a business process (such as "Product-repair cycle time"). *Input* KPIs measure assets invested to generate business results (such as "Dollars spent on research and development"). *Output* KPIs measure the results of business activities (such as "Revenues").

Check Your Knowledge: Question 3

What is a performance measurement system?

- A series of graphs showing changes in a company's performance over a specified period

  Not the best choice.

  Though a company's performance measurement (PM) system might include tools for creating graphs showing changes in performance, the correct definition of a PM system is a set of strategic objectives and performance metrics applied throughout an entire enterprise. A PM system enables executives to see how business results generated in the company's many different units combine to influence the enterprise's overall results. Thus a PM system gives executives and managers a comprehensive, high-level view of their organization's performance—and an understanding of how the company's different parts work together to produce business results.

  Commonly used PM systems include dashboards (also called cockpits) showing aggregated performance data; quality-improvement systems such as Six Sigma and the Baldrige National Quality Program; and the Balanced Scorecard.

- A centralized database containing performance data from every part of an organization

  Not the best choice.

  Though some performance measurement (PM) systems may use a database to store and report data, the correct definition of a PM system is a set of strategic objectives and performance metrics applied throughout an entire enterprise. A PM system enables executives to see how business results generated in the company's many different units combine to influence the enterprise's overall results. Thus a PM system gives executives and managers a comprehensive, high-level view of their organization's performance—and an understanding of how the company's different parts work together to produce business results.

  Commonly used PM systems include dashboards (also called cockpits) showing aggregated performance data; quality-improvement systems such as Six Sigma and the Baldrige National Quality Program; and the Balanced Scorecard.

- A set of strategic objectives and performance metrics applied throughout an entire enterprise

  Correct choice.

  Because a performance measurement (PM) system is applied throughout an entire organization, it enables executives to see how business results generated in the company's many different units combine to influence the enterprise's overall results. Thus a PM system gives executives and managers a comprehensive, high-level view of their organization's performance—and an understanding of how the company's different parts work together to produce business results.

  Commonly used PM systems include dashboards (also called cockpits) showing aggregated performance data; quality-improvement systems such as Six Sigma and the Baldrige National Quality Program; and the Balanced Scorecard.

Check Your Knowledge: Question 4

Which of the following describes the phases of the performance measurement process?

- Designing reward programs and allocating incentives to a company's business units

  Not the best choice.

  While a company may use the performance measurement process to distribute performance-based rewards fairly to employees, the performance measurement process consists of these phases: deciding what to measure, gathering performance data, and interpreting performance data.

  In the first phase (deciding what to measure), you define objectives for your group, define the actions that must be taken to achieve those objectives, then define performance metrics to help you assess whether you're accomplishing those actions. In the second phase (gathering performance data), you set targets (desired performance) for each performance metric and collect performance data. In the third phase (interpreting performance data), you analyze the data you've collected to see how the results compare to your targets, and revise your metrics and targets as needed to reflect new realities.

- Deciding what to measure, gathering performance data, and interpreting performance data

  Correct choice.

  In the first phase (deciding what to measure), you define objectives for your group, define the actions that must be taken to achieve those objectives, then define performance metrics to help you assess whether you're accomplishing those actions. In the second phase (gathering performance data), you set targets (desired performance) for each performance metric and collect performance data. In the third phase (interpreting performance data), you analyze the data you've collected to see how the results compare to your targets, and revise your metrics and targets as needed to reflect new realities.

- Selecting a formal performance measurement system, implementing it, and updating it

  Not the best choice.

  Though some companies use a formal performance measurement system, the performance measurement process does not require such a system. Instead, the process consists of three phases: deciding what to measure, gathering performance data, and interpreting performance data.

  In the first phase (deciding what to measure), you define objectives for your group, define the actions that must be taken to achieve those objectives, then define performance metrics to help you assess whether you're accomplishing those actions. In the second phase (gathering performance data), you set targets (desired performance) for each performance metric and collect performance data. In the third phase (interpreting performance data), you analyze the data you've collected to see how the results compare to your targets, and revise your metrics and targets as needed to reflect new realities.

Check Your Knowledge: Question 5

Which of the following phrases represents a performance metric?

- "Improve knowledge sharing"

  Not the best choice.

  This phrase represents an objective. The correct response is "Number of employees who complete training with passing grade by end of quarter." Performance metrics indicate how you'll determine whether you've carried out the critical activities needed to achieve your group's objectives. Metrics also indicate the kind of data you'll need to gather to evaluate performance. For example, the metric "Number of employees who complete training with passing grade by end of quarter" could enable you to assess how well you're carrying out the critical activity "Train employees on proper use of equipment," which could in turn support the objective "Reduce workplace accidents."

- "100% on-time deliveries by end of the fiscal year"

  Not the best choice.

  This phrase represents a target. The correct response is "Number of employees who complete training with passing grade by end of quarter." Performance metrics indicate how you'll determine whether you've carried out the critical activities needed to achieve your group's objectives. Metrics also indicate the kind of data you'll need to gather to evaluate performance. For example, the metric "Number of employees who complete training with passing grade by end of quarter" could enable you to assess how well you're carrying out the critical activity "Train employees on proper use of equipment," which could in turn support the objective "Reduce workplace accidents."

- "Number of employees who complete training with passing grade by end of quarter"

  Correct choice.

  Performance metrics indicate how you'll determine whether you've carried out the critical activities needed to achieve your group's objectives. Metrics also indicate the kind of data you'll need to gather to evaluate performance. For example, the metric "Number of employees who complete training with passing grade by end of quarter" could enable you to assess how well you're carrying out the critical activity "Train employees on proper use of equipment," which could in turn support the objective "Reduce workplace accidents."

Check Your Knowledge: Question 6

Which of the following would be a strategy for ensuring that you gather valid performance data on the metrics you've created?

- Accumulate data that are up to date and available frequently enough for you to track performance over time

  Correct choice.

  You can feel more confident about the validity of the data you're gathering if the data are up to date, available frequently enough for you to track performance on your metrics, and sufficiently detailed and accurate. Often, data provided by outside sources—such as organizations that track companies' market share—can also be considered valid.

- Collect data yourself on your group's performance, or have your employees collect the data as they perform their work

  Not the best choice.

  Though data that you or your employees collect personally may be relatively easy to validate, you will likely need to gather data from numerous other sources to measure performance on your metrics. For example, perhaps someone in the HR department keeps records of the number of employees who have attended and passed particular training courses.

  Regardless of the source of your data, you can feel more confident about data's validity if the data are up to date, available frequently enough for you to track performance on your metrics, and sufficiently detailed and accurate. Often, data provided by outside sources—such as organizations that track companies' market share—can also be considered valid.

- Gather only objective data—that which can be measured easily—such as sales revenue, costs, and number of new hires

  Not the best choice.

  While objective data are relatively easy to validate, you'll also want to collect subjective data such as customer satisfaction, employee morale, and a new product's innovativeness. These are important indicators of performance. Subjective data can be converted into objective form—such as customer satisfaction ratings expressed in numeric terms.

  Regardless of the original form of your data, you can feel more confident about data's validity if the data are up to date, available frequently enough for you to track performance on your metrics, and sufficiently detailed and accurate. Often, data provided by outside sources—such as organizations that track companies' market share—can also be considered valid.

Check Your Knowledge: Question 7

You want to set a target for your metric "Percentage of orders delivered on time." Which of the following approaches would you use?

- Establish a highly ambitious target—99% or 100% of orders delivered on time—to stimulate your employees' competitive spirit

  Not the best choice.

  While highly aggressive targets can activate people's competitive spirit and inspire them to excel, by themselves they can lead to discouragement and low morale if your employees feel the targets are too difficult to achieve. It's better to set a three-point range for a target—such as "80% of orders delivered on time" as your minimum acceptable performance, "90% of orders delivered on time" as your moderate level, and "99% of orders delivered on time" as your "stretch" point.

  Setting a range of targets comprising a minimum, moderate, and "stretch" point can help your employees understand the varying levels of performance they must reach in order to achieve more ambitious goals. The "stretch" point in your target range can also help get your direct

reports' competitive juices flowing: Stretch targets represent a challenge and require considerable effort.

- Benchmark on-time delivery figures in your industry, then match your target to the average on-time delivery figure you've identified

  Not the best choice.

  Though benchmarking can help you determine appropriate targets, it's more effective to set a three-point range for a target—such as "80% of orders delivered on time" as your minimum acceptable performance, "90% of orders delivered on time" as your moderate level, and "99% of orders delivered on time" as your "stretch" point.

  Setting a range of targets comprising a minimum, moderate, and "stretch" point can help your employees understand the varying levels of performance they must reach in order to achieve more ambitious goals. The "stretch" point in your target range can also help get your direct reports' competitive juices flowing: Stretch targets represent a challenge and require considerable effort.

- Set a range: 80% as the minimum target, 90% as the moderate target, and 99% as the "stretch" target

  Correct choice.

  Setting a range of targets comprising a minimum, moderate, and "stretch" point can help your employees understand the varying levels of performance they must reach in order to achieve more ambitious goals. The "stretch" point in your target range can also help get your direct reports' competitive juices flowing: Stretch targets represent a challenge and require considerable effort.

Check Your Knowledge: Question 8

You've collected data that reveal performance significantly below the target range you've set. How should you respond?

- Investigate potential causes of the shortfall, including new processes, personnel changes, and technology shifts

  Correct choice.

  Gaps between actual and targeted performance indicate the need to investigate potential causes of the shortfall. For example, if your employees are making more mistakes than the targeted numbers, the problem may stem from confusion over how to use a new technology or piece of equipment; or perhaps an unusual number of people were out on vacation during the evaluation period, and temps were brought in who weren't as familiar with the job. By identifying the causes of a performance shortfall, you can increase your chances of selecting the right intervention.

- Decide that the target range was too aggressive overall, and consider making it more moderate

  Not the best choice.

Though some targets may in fact turn out to be too aggressive, you should resist the urge to automatically lower targets when you see a performance shortfall. That approach misses the point of performance measurement.

The more appropriate response is to investigate potential causes of the shortfall. For example, if your employees are making more mistakes than the targeted numbers, the problem may stem from confusion over how to use a new technology or piece of equipment; or perhaps an unusual number of people were out on vacation during the evaluation period, and temps were brought in who weren't as familiar with the job. By identifying the causes of a performance shortfall, you can increase your chances of selecting the right intervention.

- Identify a project or initiative that will enable your group to boost performance to meet or exceed the target range

Not the best choice.

While you may eventually decide to initiate a project to address a performance shortfall, this shouldn't be your first response to a gap between actual and targeted performance. Overreacting in this way could cause you to make a drastic, expensive change that doesn't address the real reasons behind the shortfall.

The more appropriate response is to investigate potential causes of the shortfall. For example, if your employees are making more mistakes than the targeted numbers, the problem may stem from confusion over how to use a new technology or piece of equipment; or perhaps an unusual number of people were out on vacation during the evaluation period, and temps were brought in who weren't as familiar with the job. By identifying the causes of a performance shortfall, you can increase your chances of selecting the right intervention.

Check Your Knowledge: Question 9

Which of the following approaches would you use to maintain your performance measurement method?

- Keep your metrics consistent over time, so you can compare historical performance

Not the best choice.

Though keeping metrics and objectives consistent can help you compare historical performance, you need to periodically reassess these aspects of your performance measurement method to see whether they're still relevant—and change them if they're not. Business realities change—in the form of new technologies, shifting customer preferences, and new company or unit strategies. Thus, you need to strike a delicate balance between consistency and change: Keep objectives and metrics consistent where possible and appropriate, but be willing to modify them if necessary to reflect changing realities.

- Modify objectives and performance metrics if necessary to reflect changing realities

Correct choice.

Business realities change—in the form of new technologies, shifting customer preferences, and new company or unit strategies. Your objectives and performance metrics should be relevant to current business conditions. However, you want to keep your objectives and metrics as

consistent as possible over time so you can compare performance. Thus, you need to strike a delicate balance: Keep objectives and metrics consistent where possible and appropriate, but be willing to modify them if necessary to reflect changing realities.

- Change your metrics whenever you see an abrupt change in performance data

  Not the best choice.

  While an abrupt change in performance data can signal the need to revisit a metric, you shouldn't automatically adopt this response. It's better to periodically assess your objectives and metrics and modify them only if necessary to reflect changing realities—such as new technologies, shifting customer preferences, and new company or unit strategies. The ideal is to strike a delicate balance between change and consistency: Modify objectives and metrics if needed to reflect changing realities, but keep them consistent over time, where possible and appropriate, so you can compare historical performance.

Check Your Knowledge: Question 10

Which of the following is an example of a leading performance indicator?

- Customer-satisfaction ratings

  Correct choice.

  Leading indicators suggest how your group's performance might change in the future. For example, the higher your customers' satisfaction, the greater the likelihood that they'll buy from your company again as well as spend more on their purchases—thus increasing profitability. Effective performance measurement systems contain a mix of leading indicators and lagging indicators. Lagging indicators look backward at what your company has achieved in the past—for example, revenues, number of new accounts established, sales, and so forth.

- Revenues for the most recent quarter

  Not the best choice.

  "Revenues for the most recent quarter" is an example of a lagging indicator: It looks backward at what your company has achieved in the past. The correct response is "Customer-satisfaction ratings." The best performance measurement systems contain a mix of lagging and leading indicators. Leading indicators suggest how your group's performance might change in the future. For example, the higher your customers' satisfaction, the greater the likelihood that they'll buy from your company again as well as spend more on their purchases—thus increasing profitability.

- Number of new accounts established

  Not the best choice.

  "Number of new accounts established" is an example of a lagging indicator: It looks backward at what your company has achieved in the past. The correct response is "Customer-satisfaction ratings." The best performance measurement systems contain a mix of lagging and leading indicators. Leading indicators suggest how your group's performance might change in the future.

For example, the higher your customers' satisfaction, the greater the likelihood that they'll buy from your company again as well as spend more on their purchases—thus increasing profitability.

Check Your Knowledge: Results

Your score:

Steps for measuring performance

1. **Define your group's objectives.**

   With your employees and boss, identify three to five objectives that, if achieved, would best enable your group to contribute to your organization's strategic direction, solve pressing business problems, or serve customers better. Express your objectives in short phrases that start with a verb—for example, "Reduce workplace accidents," "Improve knowledge sharing," or "Increase sales per employee."

2. **Define critical success factors for each objective.**

   For each objective, identify two or three actions that would best enable your group to accomplish that objective. These are your critical success factors (CSFs). To illustrate, for the objective "Reduce workplace accidents," your CSFs might be "Train employees to use equipment properly," "Provide safety equipment and apparel," and "Regularly inspect workshop for compliance with safety rules."

3. **Translate critical success factors into performance metrics.**

   Break down critical success factors into one or more metrics, describing them in language that reflects how you'll measure performance in the factor.

   > For example, one measurement for the critical success factor "Train employees on proper use of equipment" could be "Number of employees who complete training with passing grade by end of quarter." For the CSF "Provide safety equipment and apparel," you might choose these two metrics: "Percentage of personnel who have adequate inventory of safety equipment and apparel," and "Frequency of equipment and apparel vendors' notification of safety product updates."

4. **Set targets for your performance metrics.**

   For every performance metric you've defined, set a target representing the desired performance on that metric. Use historical performance data (such as the current period's performance or the previous year's average) to set a baseline, or starting point, for your targets. Where no historical data exist, use industry benchmarks, discussions with your employees, and knowledge of your direct reports' capabilities to determine appropriate targets.

   Consider setting a three-point range—minimum, moderate, and "stretch" targets—for a particular metric, so employees can see the minimum performance they need to reach on their way to achieving more ambitious goals.

For example, for the metric "Number of employees who complete training with passing grade by end of year," you might set a minimum target of 80%, a moderate target of 90%, and a stretch target of 100%.

5. **Collect performance data.**

   Gather data on actual performance on the metrics you've defined. Data sources might include managers in other departments (for example, IT may have information on customer loyalty scores), your employees, and third-party organizations (such as training consultants) that keep records you need. Many industry research firms and consultants also conduct proprietary benchmarking surveys; ask your boss if your company participates in such surveys.

6. **Analyze performance data.**

   Review the actual performance data you've gathered, and compare the results to your target (desired) performance. Decide what to do about any gaps. A gap between actual and desired performance may suggest the need for a new project or initiative to improve employees' capabilities or correct a faulty process. A gap may also indicate that you've set an overly aggressive target. Other possibilities are that data are unreliable or inaccurate.

   Investigate the real cause behind the gap and address it through appropriate measures. Resist any urge to automatically lower targets to close performance gaps. Likewise, don't immediately launch a costly, time-consuming initiative to address performance shortfalls, if the data are trending in the right direction.

7. **Test your measurement system.**

   Ask whether any performance metrics should be changed to more accurately represent the objective you're trying to achieve, and whether targets need to be revisited. Abrupt changes in performance data, as well as new processes, can indicate the need to revise your metrics or targets.

   For example, a new technology that reduces the time needed to fill vacant positions from months to weeks or days may render your metric "Number of months to fill vacant positions" (and its corresponding target of "Two months") irrelevant.

Steps for communicating performance data to your group

1. **Review your group's performance data.**

   Gather all the reports, forms, and other documents in which your group's performance data are recorded for the period in question. Review the data, looking for places where actual performance differs from the targets you set.

2. **Craft a story about what's happening.**

   Based on what you're seeing in your group's performance data, develop a narrative describing what's happening with performance. Highlight interrelationships between metrics, and note possible explanations for why actual performance is differing from targeted performance.

   For example, "We're having trouble reaching our targeted 3% error rate, and that's negatively affecting customer satisfaction and costs. New hires and order-processing software may have played a part in raising the error rate these past two months."

Seek others' ideas about the underlying causes of performance problems. Peer managers, your boss, and some of your employees may have valuable insights into what's going on.

3. **Create charts and graphs.**

   Where possible, translate numerical information into simple charts and graphs that capture trends.

   > For example, a line graph showing an increase in error rate over the past six months can prove far more compelling than a list of numbers.

   Also, snapshot views are handy for senior management. Thus, if you will be sharing performance results with them, they will appreciate receiving information in such a succinct way.

4. **Select the appropriate degree of detail.**

   Consider what your employees need to know about the group's performance in order to make improvements. Decide whether the story you've crafted and the charts and graphs you've prepared contain the right degree of detail to make your point. Too much detail, and your employees may become confused or lose interest. Too little detail, and they may not grasp the importance of a performance problem.

5. **Communicate difficult facts constructively.**

   Even if your narrative, your charts and graphs, and the details you've gathered about your group's performance present a discouraging picture, it's important to communicate the truth about performance to your employees. However, in communicating the information, strive to do so constructively. That is, don't single out individuals as the cause behind poor group performance. Instead, look for the problematic processes and systems behind the shortfalls and explore ideas for addressing them.

6. **Create opportunities for review and discussion.**

   Set up meetings and review sessions with your group to specifically discuss performance results and changes made to address them. Together, explore what has worked well and what hasn't. Encourage your employees to adopt a mindset of continual, collective improvement.

Tips for launching the performance measurement process

- Enlist subject-matter experts. Identify internal subject-matter experts who may have insights into the aspects of your group's performance that you want to measure.

  > For example, if you're dealing with a turnover problem, consider asking someone in the human resources department for their views on how best to measure turnover and set realistic turnover targets. They'll have a broader view, and access to information on industry workforce trends.

- Consult with performance measurement (PM) system managers. If your company uses a performance measurement system that is managed by a special team or department, ask the system manager or administrator for advice on how to track—and analyze—your group's performance.
- Organize a task force. Assemble a group of peer managers and employees who can help you brainstorm ideas for objectives, metrics, targets, and so forth. Make it clear that the group's

effort is iterative: You may need to fine-tune or dramatically revise ideas after testing them under actual conditions.

- Consider external data sources and resources. Use industry benchmarking data and other external information sources to define objectives, metrics, and targets. Take advantage of the information available from your larger industry community and from the large and growing performance management community, through conferences, seminars by private business groups, and associations.

  For instance, if turnover rates in your industry tend to be higher than in other industries, you could feel fairly confident that a similarly high turnover rate in your group constitutes acceptable performance. Just be careful to compare yourself with a peer group: a 10% turnover rate in a company of 100 employees has far greater impact than the same rate in an organization of 1,000.

- Emphasize the ultimate goal: a constructive, not punitive, effort. The primary goal of performance measurement is not to assign blame, but to identify and solve performance problems and to seek constant improvement in every aspect of your team's work—especially those that directly impact the achievement of company strategy. When you emphasize this, employees are more likely to support the effort and participate actively, rather than try to cover themselves or, worse, sabotage the effort.
- Analyze your results. Assemble a task force to review and analyze performance results over time. You'll need your task force's help in validating whether your objectives and metrics are still relevant. You'll also want to assess your reporting mechanism: Does it measure at the proper frequency? How much time and effort does it take? How helpful is its format? What improvements can be made?

  Another issue to consider: the impact of the measurement process itself on your team members' behavior and individual performance. Are people "on board"? Wary? Confused about how the process works? Address any difficulties in these areas as soon as possible.

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Tips for defining objectives

- Brainstorm effectively. While meeting with colleagues and direct reports to brainstorm objectives, stress the importance of active participation by everyone. Encourage people to generate as many ideas as possible without judging them, and capture all ideas on a flip chart or other visual recording device. If people start running out of steam, invite them to get up, walk by the flip chart, and add one more idea. Often, a little physical activity can reenergize people. Be willing to hold additional brainstorming sessions if necessary to generate sufficient ideas. Offsite meetings are a good way for people to get a fresh perspective on the business and business processes.
- Begin each objective with an action verb. Using verbs such as "Increase," "Reduce," "Initiate," "Develop," "Lower," "Improve," "Become," "Achieve," and so on helps distinguish the action-oriented nature of objectives from the sometimes static world of strategy. An objective that starts with an action verb answers the crucial question of how your group's strategy will be executed.

  For example, a strategy of operational efficiency could translate into the following objectives: "We will execute our strategy of operational efficiency by lowering costs, increasing loyalty, reducing rework, and closing skills gaps."

- Don't worry about making your objectives quantitative. Metrics require numerical representations of success. Objectives don't.
- Ensure a shared understanding of your objectives' meaning. Work with your direct reports to clarify the meaning of each objective.

  For example, the objective "Close skill gaps" could be interpreted in numerous ways. Gain consensus from your people on what closing skill gaps means in practical terms: What skill gaps, in particular, will you seek to close? How will you close them—through training, recruitment, or some other means? Answers to such "how" questions can also help you define your critical success factors (CSFs)—which you'll later translate into performance metrics.

- Verify the relevance of your objectives. Review your objectives and ask yourself how consistent they are with your group's strategy and values. Ask: "Will achieving these objectives help us execute our strategy and be true to our values?"

Tips for creating performance metrics

- Start with your objectives and critical success factors. For each objective you define, list two or three actions that would best enable your group to achieve that objective. These actions become your critical success factors (CSFs). Translate each CSF into one or more performance metrics.

  For example, the CSF "Improve retention" could be translated into the performance metric "Percentage of new hires who stay beyond their first year."

- Look beyond financial measures. Ensure that your set of metrics reflects the nonfinancial as well as the financial aspects of your group's performance.

  For example, do you have metrics for nonfinancial matters such as process efficiencies, employee knowledge, and customer experiences?

- Identify cause-and-effect linkages. Examine your set of metrics for cause-and-effect connections.

  For example, how will good performance on the metric "Number of order-processing errors" affect performance on the metric "Customer satisfaction" or "Employee morale"? What's the strength of these relationships? For instance, will you need just a small improvement in error reduction to generate a large improvement in customer satisfaction?
  The more cause-and-effect linkages between your metrics—and the deeper your understanding of the relative strength of these linkages—the more comprehensive picture you'll have of your group's performance.

- Examine your lagging/leading mix. Review your set of metrics. Ask whether you they show a mix of lagging (backward-looking) and leading (forward-looking) indicators. Your set of metrics should contain both lagging and leading indicators.
- Strive for a balance of subjective and objective metrics. Determine whether your metrics reflect both subjective (such as customer satisfaction) and objective (for example, revenues) indicators. If not, revise your metrics so that they show a mix of these two types of indicators.
- Consider availability, validity, and reliability of data. For each metric, ask yourself whether data exist to track performance on that metric, and whether the data will be reliable. A performance

metric is useless if you can't gather the required data or depend on the data to be up-to-date and accurate.

- Draw on internal and external data. In addition to analyzing information within your organization (such as sales figures), examine data outside your company (such as third-party ranking of companies' performance against competitors').
- Use clear, accessible language. Phrase your performance metrics in specific, concrete, and easy-to-understand language—such as "Number of late deliveries per month" instead of "Service quality."

Tips for setting performance targets

- Establish a three-point range of targets for your metrics. These three types of targets can work together to shape your group's future performance.

  For example, a minimum target of "12% error rate" can feel more manageable to employees and help them gain the positive results and confidence to meet your moderate ("9% error rate") and even "stretch" ("4% error rate") targets.

- Involve your employees. Your direct reports are closest to the action and in the best position to provide information on what's possible in their work. Involve them in setting targets—you'll gain their buy-in as they feel a sense of ownership in the process.
- Consider trends to establish a target baseline. If past data exist for performance on a particular metric, examine that data for trends that can serve as a baseline for setting targets for future performance.

  For example, suppose you want to set a target for employee turnover over the coming six months, and turnover rates for your group have climbed slowly from 2% to 7% over the previous two years. In this case, a target of reducing turnover from 7% to 4% in the next six months may make sense and be realistic.

- Get your boss's input. Ask your boss for ideas about what level of performance on each metric might best enable your group to achieve its objectives. Your boss may have some helpful suggestions based on his or her experience and understanding of unit and company goals.
- Use SWOT analysis. Consider your group's internal strengths and weaknesses, as well as its external opportunities and threats. Ask yourself what targets would enable your group to build on its strengths and leverage opportunities, as well as minimize weaknesses and threats.

  For instance, if your group is particularly knowledgeable about your company's products, perhaps the ambitious target of "25% increase in customer loyalty by quarter end" is perfectly realistic and achievable.

- Gather feedback from customers and other stakeholders. Expectations from these groups might yield insights you can use to set targets.

  For example, by asking customers what constitutes great performance in their minds, you can generate targets that will meet or even exceed their performance requirements.

- Consider industry averages. Numerous credible agencies monitor performance of specific industries—for example, J.D. Power & Associates tracks many industries. Review these performance ratings, and decide whether they can inform your targets.

  For instance, if error rates in an industrywide manufacturing process that your company uses range from 5% to 10%, those figures may serve as a reasonable target for your

error-rate metrics.

- Identify initiatives. While considering targets, ask yourself what new projects or change efforts may be required to support achieving your targets.

    For example, to meet a target of "100% on-time delivery of orders," will your employees need a new software application to track fulfillment processes? Will they need training on the new system?

Worksheet for understanding key performance indicators

Worksheet for Understanding Key Performance Indicators
Use this worksheet to identify and understand your company's and unit's key performance indicators (KPIs).
1. What are your company's high-level goals? *Consider the type of organization you work for, its mission, and its strategy. For example, if your company is global, perhaps a high-level goal is to expand sales in international markets. If your organization is a social service nonprofit, maybe a goal is to reduce the ratio of administrative costs to total donations received. If you're not sure of your company's high-level goals, ask your boss for clarification.*
2. What measurements does your company use to assess how well it's achieving its high-level goals? *These measurements are the company's key performance indicators. Examples may include "Percentage of income deriving from international markets," "Total administrative costs as a percentage of donations received," "Return on investment," "Economic value added," and "Breakeven time." If you're not sure which KPIs your company uses, ask your boss for advice. Most companies have three to four KPIs.*
3. Of your company's key performance indicators, which are input KPIs? Which are process KPIs? And which are output KPIs? *Input KPIs might include investments in research and development, funding for employee training, quality of raw materials, and other assets and resources used to generate business results. Process KPIs might encompass order delivery time, time to fill vacant positions, product repair cycle time, and other efficiency-related measurements. Output KPIs might include revenues, return on investment, economic value added, breakeven time, revenues, number of new customers, and other results of business activities.*
4. What KPIs has your unit defined? *Each unit has different KPIs tailored to its function within the company. For instance, the customer service department probably tracks the number of customers served during a given time period. The product development unit likely assesses the number of new offerings introduced and the ratio of new to existing products. And the human resources unit probably measures workforce skill levels, hiring efficiency, and other human capital related activities.*
5. Which of your unit's KPIs are input? Process? Output? *See the examples in question 3 for reminders.*
6. In what ways do your unit's KPIs relate to and support your company's KPIs? *For example, suppose you work for a global consumer goods company that has a KPI "Percent income deriving from international markets," and you lead a group in the adult apparel unit. In this case, your unit's KPIs might include "Number of satellite offices established in Europe," "Total sales for Europe, Middle East/Africa, and Asia," and other KPIs related to your company's goals.*

Worksheet for understanding your company's performance measurement system

Worksheet for Understanding Your Company's Performance Measurement System

Use this worksheet to identify and understand the performance measurement approach your company uses.

1. What aspects of business performance does your company measure? *For example, does it measure improvements in all business processes (manufacturing, product development, order fulfillment, customer service), or just some—and if so, which ones? Does it assess the effectiveness of solutions to problems? Does it look beyond financial indicators to assess nonfinancial "perspectives" on business performance such as workforce learning, process efficiency, and customer service? Does it track performance on criteria such as knowledge management, customer focus, leadership quality, and strategic planning? If you're not sure, talk with someone in the unit or team responsible for measuring performance.*

2. What kinds of performance data does your unit routinely gather? And how is this data used to help form a picture of overall company performance? *If you're unsure, ask your boss for his or her insight.*

3. Has your company adopted a formal performance measurement (PM) system? If so, what is it? *Common PM systems include a dashboard or cockpit, as well as quality-improvement systems such as Plan-Do-Check-Act, Six Sigma, and the Baldrige National Quality Program. The Balanced Scorecard is another widely used performance measurement system; many companies use it to understand the relationship among nonfinancial performance and financial results, and to better manage strategy execution. If you're not sure whether your company uses a formal PM system or which system it uses, ask your supervisor for clarification.*

4. How is performance data from each unit in your company entered into the company's PM system? *Do unit managers collect data from group leaders such as yourself, aggregate the data on spreadsheets, and e-mail the documents to the PM system team? Is there an internal Web site that unit managers can use to input the aggregated performance data?*

5. What kinds of performance reports does your company's PM system generate? *Does the system produce monthly or quarterly company-level results broken down by unit? Are results coded in some way to indicate how they compare with performance targets? For example, do reports use a "traffic light" system—coding on-target or above-target performance as green and problem performance as yellow or red?*

6. How does your unit use the performance information generated by the company's PM system? *Who has access to the information? Do unit leaders such as your boss meet regularly with group leaders to discuss performance results?*

Worksheet for deciding which performance aspects to measure

Worksheet for Deciding Which Performance Aspects to Measure

Use this tool to define objectives for your group, identify critical success factors (CSFs) for each objective, and translate your CSFs into performance metrics. This tool is especially helpful if your company does not use a formal performance measurement system.

1. What does your group need to achieve in order to contribute to your company's performance? *Consider ways in which your group can support your unit's or company's strategy, solve recurring business problems, serve customers better, and acquire needed skills or knowledge. Brainstorm as many ideas as you can.*

2. Of the needed achievements you listed in step 1, which do you consider *most* important? Why? *Try to whittle your list down to about five to seven items. These become your group's objectives.*

3. Look at each objective you listed in step 2. For each objective, identify the two or three actions that would *best* enable your group to accomplish that objective. *These become your critical success factors (CSFs). For example, if one of your objectives is "Improve knowledge sharing," your CSFs might include "Improve new-hire mentoring" and "Establish job-shadowing relationships." Note your ideas in the table below. Ask your employees or colleagues for ideas, too—the people closest to each process or task can often provide helpful insights.*

Objective	**Critical Success Factors**

4. Look again at each CSF you listed in step 3. Express each CSF as one or more performance metrics. *For instance, th CSF "Improve new-hire mentoring" could be translated into the performance metrics "Percentage of new hires this year who have mentors assigned by their start date" and "New hires' knowledge of company policies and job responsibilities." List each CSF and its corresponding performance metric(s) in the table below.*

Objective 1:

Critical Success Factor	**Corresponding Performance Metric(s)**

Objective 2:

Critical Success Factor	**Corresponding Performance Metric(s)**

Objective 3:

Critical Success Factor	**Corresponding Performance Metric(s)**

Objective 4:

Critical Success Factor	**Corresponding Performance Metric(s)**

Objective 5:

Critical Success Factor	**Corresponding Performance Metric(s)**

Worksheet for setting performance targets

Worksheet for Setting Performance Targets

Use this tool to set performance targets for the metrics that you've created for your group or that your boss has defined for your group based on the company's formal performance measurement system.

- In the first column of the table below, list the performance metrics established for your group.
- In the second column, write a range of possible targets.
- In the third column, note your rationale for the target ranges you're proposing. Possible influences on your choice of target may include benchmarks (such as targets considered reasonable by other companies in your industry) as well as historical data that can serve as a baseline for your target.

Metric	Possible Targets	Rationale
Example: *Percentage increase in customer satisfaction by year end*	***Example:*** *Minimum: 5%* *Moderate: 8%* *Stretch: 10% increase in customer satisfaction by year end*	***Example:*** *10% is a bit aggressive but may stimulate my group's competitive spirit. We have the systems, skills, and commitment in place to push for this stretch target. Also, over the past year, customer satisfaction picked up during the third and fourth quarters. I think we've got some momentum going that we can use to achieve these increases.*

Worksheet for tracking performance results

Worksheet for Tracking Performance Results

Use this tool to track your group's performance results over several evaluation periods and to document thoughts about how to interpret and respond to the results.

- In the first column in the table below, list the performance metrics established for your group.
- In the second column, record the target you've set for each metric.
- In the next three columns, record the actual performance for each metric over each evaluation period.
- In the final column, record your thoughts about what the performance data seem to be indicating and how you might best respond to the data.

Metric	Target	Performance Data			Notes
Example: *% of one-call resolutions of customer complaints*	***Example:*** *75% per month*	***Example:*** *Jan. 55%*	***Example:*** *Feb. 65%*	***Example:*** *Mar. 55%*	***Example:*** *Investigate drop in performance during March. Possible causes: we were short staffed because several people were out on vacation; installed new phone system that some people had difficulty learning to use.*

Why Develop Others?

"At the end of the day, you bet on people, not strategies."
Larry Bossidy
Former CEO, AlliedSignal

In today's global business environment, markets and regulations change quickly. Competitors constantly innovate. Technological changes are the norm.

In order to outmaneuver the competition and meet the demands of the moment, organizations must be agile. They must execute flawlessly. And they must transform themselves continuously.

Are your leaders ready?

Dr. Noel M. Tichy
Professor
University of Michigan Ross School of Business

We have now entered an era where I don't care what industry you're in, you need leaders who can make decisions, make judgment calls at every single level. All the way down to the interface with the customer.

If you go to a company like Google or any of the high tech companies, a lot of the innovation that Amazon does is happening right at the front line. Go ahead, try it, put it out there, we'll learn from it. That cannot happen if the senior leadership doesn't have a commitment to both develop the leadership capability, but develop the business through engaging people at all levels of the organization.

Becoming a teaching organization

I like to tell parents that they cannot delegate their responsibility to develop their children. And I think it is the same in an organization. Day in and day out the person that has the biggest impact on people in the organization is the next level above and the associates around and below.   And so to build a learning organization I say is not enough. Learning could be, you know we are learning cooking, we are learning this or that, but teaching organizations, when I learned something, I have a responsibility to teach my colleagues.

So everybody takes responsibility for generating new knowledge and it is not enough to be a learner, you then have to translate it into teaching.

The Virtuous Teaching Cycle
The role of a leader is to ensure that the people who work for them and around them are better every day. There's only one way to make people better. It's to teach them, learn from them, create what I call "virtuous teaching cycles”, not command and control.

A virtuous teaching cycle is teach learn, teach learn. And the leader has a responsibility for reducing the hierarchy, for having a point of view to start the discussion, but then to be responsible to hear everyone's voice, get everyone involved in a disciplined way. It is not a free for all. But it is the leader's responsibility to create that virtuous teaching cycle.

A wonderful example of virtuous teaching cycle is the program that Roger Enrico ran at Pepsi, where every one of the 10 vice presidents comes with a business project.

Roger Enrico gets smarter as result of five days with 10 vice presidents, because he's learning from them. He needs to lower the hierarchy. He needs to be open to learning. And in turn, the people participating need to be energized and empowered to come up and engage in problem solving.

Another example is at Best Buy, where every morning in the stores you would bring 20 associates or so together and they would review the profit and loss statement from the day before, what we learned from the different customer segments in our stores, what we can do to improve our performance this day. And they do that every single day. The store manager was learning mostly from the associates on the floor.

That was a virtuous teaching cycle were everybody is teaching everybody, everybody is learning and the result has been an incredible result at Best Buy.

“The growth and development of people is the highest calling of leadership.”
- Harvey S. Firestone
    Founder, Firestone Tire and Rubber Co

There are clear advantages to leader-led development.

But for many leaders, taking on teaching, coaching, and other development responsibilities can seem daunting. You might avoid taking on these roles due to lack of time, resources, or your own lack of comfort with this role.

The following tips and resources can help you impart valuable learning to your team every day.

To develop others...

- Start with a Teachable Point of View

The first requirement of being able to develop other leaders is to have what I call a teachable point of view. I often give the example of, if I ran a tennis camp and you just came to day one of the tennis camp, I better have a teachable point of view on how I teach tennis. So you are standing there looking at me and it has got four elements. One, the ideas, well how do I teach the backhand, the forehand, the serve, rules of tennis. Then if I am a good tennis coach, I have a set of values. What are the right behaviors I want, how do I want you to dress, how do I want you to behave on the tennis court.

But if that's all I have, what do I do? Show you a power point presentation and then expect you to hit 500 backhands, 500 serves, run around for eight hours. I have to have a teachable point of view on emotional energy. How do I motivate you to buy in to the ideas and values?

On one end of the spectrum it could be I threaten you with corporal punishment, the other I can give you stock options, I can make you feel good about yourself, I can help you develop as a human being, what motivates you.

And then finally, how do I make the tough judgment calls, the yes/no, decisions as the tennis coach, the ball is in, the ball is out. I don't hire consultants and set up a committee, it is yes/no. And the same with running a business, what are the products, services, distribution channels, customer segments that are going to grow top line growth and profitability of the organization.

What are the values that I want everyone in the organization to have, how do I emotionally energize thousands of people, and then how do I make the yes/no, judgments on people and on business issues. So the fundamental building block of being able to develop other leaders is to have that teachable point of view just like the tennis coach.

To develop others...

- Lead with questions

Questions are hugely important because you want to create dialogue and again, what I call a virtuous teaching cycle where the teacher learns from the students and vice versa. Which means everybody ought to be free to ask whatever is on their mind, whatever it will take to get clarity and understanding, but it is not the leader just coming in and freeform asking questions. I believe the leader has a responsibility for framing the discussion, for having as best they can a teachable point of view, they may need help from their people in flushing it out, but they need to set the stage but then it has to be a very interactive, what I call virtuous teaching cycle environment, teach learn, teach learn, teach learn.

To develop others...

- Make it part of your routine

A good example to me of an outstanding leader developing other leaders is Myrtle Potter who at the time I am commenting was Chief Operating Officer of Genentech running the commercial side of the business. And she would take time at the end of every single meeting and do some coaching of the whole team on how we could perform as a team better, and then she would often take individuals and say, could we spend 10 minutes over a cup of coffee, I want to give you some feedback and coaching on that report that you just presented on or how you are handling a particularly difficult human resource issue, but it was part of her regular routine. And I think the challenge for all of us as leaders is to make that a way of life and it is built into the

fabric of how we lead and it is not a one off event, three times a year. It is happening almost every day.

To develop others...

- Make it a priority

One of the biggest challenges in getting people kind of on this path is to overcome some of their own resistance, either fear or the way I view the world I don't have time for this, everybody can make time. Roger Enrico is CEO of Pepsi. He didn't have time to go off for a week at a time and run training sessions. He had to readjust his calendar. So it requires you to look in the mirror and say, is this important. If it is important, of course I can make the time. Then I have to get over my own anxiety on how well I can do it, but it is a commitment to get on the path that says: this is how I am going to drive my own performance and the performance of my colleagues.

To develop others...

- Learn to teach

I think the biggest mistake is to assume you are going to be good at it right off the bat. It is like learning anything else. First time you go out and try and play tennis, good luck. But you got to stay with it and you got to engage your people in helping make you better and them better. And so it is a journey you need to get on, not I am going to do it perfectly when I start out.

If you want to be a great leader who is a great teacher, it's very simple. You have got to dive into the deep end of the pool. But you've got to dive into the pool with preparation. I don't want you drowning. I want you succeeding. It is extraordinarily rewarding for most human beings to teach others. I think once you can turn that switch on, it is self perpetuating. You get a lot of reinforcement, your team is better. You perform better because your performance goes up and it becomes this virtuous teaching cycle.

Your opportunity to develop others

We’ve heard why developing others can drive greater business results, and how to make the most of your leader-led development efforts. The materials provided in Develop Others enable you to create personalized learning experiences for YOUR team within the flow of their daily activities. Use the guides and projects to engage your team quickly. And to explore how key concepts apply to them in the context of their priorities and goals.

The value of teaching is the performance of the organization is totally dependent on making your people smarter and more aligned every day as the world changes. In the 21st century we are not going to get by with command and control. We are going to have to get by with knowledge creation. The way you create knowledge in an organization is you create these virtuous teaching cycles where you are teaching and learning simultaneously, responding to customer demands and changes, responding to changes in the global environment. My bottom line is if you're not teaching, you're not leading.

A leader’s most important role in any organization is making good judgments — well informed, wise decisions about people, strategy and crises that produce the desired outcomes. When a leader shows consistently good judgment, little else matters. When he or she shows poor judgment nothing else

matters. In addition to making their own good judgment calls, good leaders develop good judgment among their team members.

Dr. Noel M. Tichy
Professor, University of Michigan Ross School of Business

Dr. Noel M. Tichy is Professor of Management and Organizations, and Director of the Global Business Partnership at the University of Michigan Ross School of Business. The Global Business Partnership links companies and students around the world to develop and engage business leaders to incorporate global citizenship activities, both environmental projects and human capital development, for those at the bottom of the pyramid. Previously, Noel was head of General Electric's Leadership Center at Crotonville, where he led the transformation to action learning at GE. Between 1985 and 1987, he was Manager of Management Education for GE where he directed its worldwide development efforts at Crotonville. He currently consults widely in both the private and public sectors. He is a senior partner in Action Learning Associates. Noel is author of numerous books and articles, including:

For more information about Noel Tichy, visit http://www.noeltichy.com.

Share an Idea

Leaders are in a unique position to recognize the ideas and tools that are most relevant and useful for their teams. If you only have a few minutes, consider sharing an idea or tool from this topic with your team or peers that is relevant and timely to their situation.

For example, consider sending one of the three recommended ideas or tools below to your team with your comments or questions on how the idea or tool can be of value to your organization. By simply sharing the item, you can easily engage others in important conversations and activities relevant to your goals and priorities.

Steps for measuring performance
Tips for setting performance targets
Guidelines for interpreting performance data

To share an idea, tip, step, or tool with your comments via e-mail, select the EMAIL link in the upper right corner of the page that contains the idea, tip, step, or tool that you wish to share.

Discussion 1: Deciding what to measure

When your team members measure their collective performance, they generate important forms of value for your organization. For one thing, they can spot — and promptly address — problems. They can also determine whether their team is meetings its goals and whether it needs to revise its budgets and forecasts. And they can get a better sense of how they're doing compared to the competition — and take steps as needed to gain a competitive edge.

But measuring a group's or organization's performance is challenging. Your team members may be saying to themselves, "I know we need to assess our performance. But we do so many different things in our group. What, exactly, should we be measuring?"

Effective performance measurement starts with three steps: (1) defining important objectives your team must achieve to support the organization's efforts, (2) articulating "critical success factors" (CSFs), the actions the team must take to achieve those objectives, and (3) selecting metrics for

assessing how well the team is accomplishing its CSFs.

Use these resources to lead a discussion with your team about how to accomplish these steps in the context of your team and organization.

Download resources:

Discussion Invitation: Deciding What to Measure
Discussion Guide: Deciding What to Measure
Discussion Slides: Deciding What to Measure (optional)
Tips for Preparing for and Leading the Discussion

Working through the discussion guide can take up to 45 minutes. If you prefer a shorter 15- or 30-minute session, you may want to focus only on those concepts and activities most relevant to your situation.

Discussion 2: Performance measurement pitfalls

When your team members measure their groups' collective performance, they can fall victim to several common pitfalls. For example, perhaps they're relying on just one metric to measure the group's overall performance (which gives a distorted picture of what's going on) or they've defined too many metrics (which creates confusion). Or maybe they're focusing on objectives that don't align with any important company goals. Thus they're measuring — and trying to improve — performance that doesn't really contribute to your organization's success.

By identifying performance measurement pitfalls they may be facing, your team members can more easily generate ideas for avoiding them — and lay the groundwork for effectively assessing their respective groups' overall performance.

Use these resources to lead a discussion with your team about how to spot and avoid performance measurement pitfalls.

Download resources:

Discussion Invitation: Performance Measurement Pitfalls
Discussion Guide: Performance Measurement Pitfalls
Discussion Slides: Performance Measurement Pitfalls (optional)
Tips for Preparing for and Leading the Discussion

Working through the discussion guide can take up to 45 minutes. If you prefer a shorter 15- or 30-minute session, you may want to focus only on those concepts and activities most relevant to your situation.

Start a Group Project

Just like any change effort, successfully incorporating new skills and behaviors into one's daily activities and habits takes time and effort. After reviewing or discussing the concepts in this topic, your direct reports will still need your support to fully apply new concepts and skills. They will need to overcome a variety of barriers including a lack of time, lack of confidence, and a fear of making mistakes. They will also need opportunities to hone their skills and break old habits. To help ensure their success, you can provide safe opportunities for individuals and your team as a whole to practice and experiment with new skills and behaviors on the job.

For example, to encourage the adoption of new norms, you can provide your team members with coaching, feedback, and additional time to complete tasks that require the use of new skills. Management approaches such as these will encourage team members to experiment with new skills until they become proficient.

Group learning projects provide another valuable technique for accelerating team members' development of new behaviors. A group learning project is an on-the-job activity aimed at providing team members with direct experience implementing their new knowledge and skills. Through a learning project, team members discover how new concepts work in the context of their situation, while simultaneously having a direct and tangible impact on the organization.

The documents below provide steps, tips, and a template for initiating a group learning project with your team, along with two project recommendations for this topic.

Download resources:

Tips for Initiating and Supporting a Learning Project
Learning Project Plan Template
Learning Project: Measure Our Team's Performance
Learning Project: Get to Know Our Organization's Performance Measurement System

The Five Traps of Performance Measurement

Andrew Likierman. "The Five Traps of Performance Measurement." *Harvard Business Review*, October 2009.

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Summary

Evaluating a company's performance often entails wading through a thicket of numbers produced by a few simple metrics, writes the author, and senior executives leave measurement to those whose specialty is spreadsheets. To take ownership of performance assessment, those executives should find qualitative, forward-looking measures that will help them avoid five common traps: Measuring against yourself. Find data from outside the company, and reward relative, rather than absolute, performance. Enterprise Rent-A-Car uses a service quality index to measure customers' repeat purchase intentions. Looking backward. Use measures that lead rather than lag the profits in your business. Humana, a health insurer, found that the sickest 10% of its patients account for 80% of its costs; now it offers customers incentives for early screening. Putting your faith in numbers. The soft drinks company Britvic evaluates its executive coaching program not by trying to assign it an ROI number but by tracking participants' careers for a year. Gaming your metrics. The law firm Clifford Chance replaced its single, easy-to-game metric of billable hours with seven criteria on which to base bonuses. Sticking to your numbers too long. Be precise about what you want to assess and explicit about what metrics are assessing it. Such clarity would have helped investors interpret the AA ratings involved in the financial meltdown. Really good assessment will combine finance managers' relative independence with line managers' expertise.

Target Setting

Robert Kaplan. "Target Setting." *Balanced Scorecard Review*, May 2006.

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Summary

Articulating strategy and identifying strategic objectives often get the spotlight as major scorecard-building challenges. But defining measures and setting targets are no less challenging—for different reasons. And unlike the more stable Balanced Scorecard (BSC) elements, targets must, by definition, be continually revised. One of the most delicate tasks is setting effective stretch targets—those that are ambitious, yet achievable, without being demoralizing. The implications are great, not just for company performance but for individual performance and morale. Here, Robert S. Kaplan discusses external and internal benchmarks across the four BSC performance perspectives, presenting proven methods for setting stretch targets that deliver the results leaders want without incentivizing the wrong behavior.